A. J. DANKS

what everyone should know about social credit

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FIVE SHILLINGS

WHAT EVERYONE SHOULD KNOW ABOUT SOCIAL CREDIT

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A. J. Danks

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INTRODUCTION

I am sorry to fly in the face of the ordinary New Zealander's cherished, and thoroughly exercised, right to grumble about his economic circumstances. But it must be admitted that this country has, over the past ten years or so, lived through a time of prosperity without equal in our history. Even wishful thinking about how pleasant pre-war prices were, especially in mental association with post-war incomes, should not disguise from us the undoubted fact that even if things *could* be better, they usually have been a great deal worse: we have much to be thankful for.

It is, therefore, remarkable that the Social Credit Movement, which suggests that more inflation is what is wanted for an already inflated economy, should have received as good a hearing as it did at the recent elections. The common sense of economic developments in New Zealand for years past is that we have had too much, rather than too little, purchasing power. More money, in the form of a Social Credit dividend, must be matched by more goods, if prices are not to rise. Where are these factories which are idle, these empty houses, these unemployed workers, these spare resources which are waiting, like the Sleeping Princess, to be kissed to life by the Social Credit Prince Charming? Common sense says that they are simply not there.

Unfortunately, people are apparently not willing to trust the simple view. A complicated economic argument is used by social credit to persuade that a 'gap' is there. And the promise of the hand-outs of the social credit dividend is a strong inducement to many to hasten through the intellectual barbed wire of the economics into the world of promise beyond.

This short study is aimed at those who are prepared to stop and think before accepting what I am sure is a fool's paradise. The intellectual barbed wire is, I am afraid, quite prickly, and the reader will need patience as I try to snip it, strand by strand. But those who will stay with the text through the necessarily slow going on the A plus B theorem will find their interest quickened,

as the argument develops, with discussions of Slumps, Money, Interest, and other topics of current importance.

Two omissions need brief explanation. I have, in the first place, written practically nothing about social credit in Canada. This is simply because the federal system of government in that country does not devolve the powers of monetary reform into the hands of the social credit provincial governments of Alberta and British Columbia. The Canadian experiment is, therefore, an exercise in the politics of monetary reform, conducted meantime without the powers necessary to make such reform politically practicable. One can imagine that this may well strengthen the parties in Alberta and British Columbia; they are not called upon to live up to their promises, and they have a good political excuse for doing anything financially unpopular: it is forced on them by powers outside their control.

It should be noted that we have no constitutional barrier in New Zealand to save us from the monetary reformers. A social credit government here could launch out into financial experiments by ordinary legislation. So, as I have pointed out in the text, it is much better to prove social credit wrong by wisdom before the event, than to await the inevitable disastrous inflation which would be the price of a political proof.

Finally, I have not been able to deal with the much publicised figure of £193½ million of 'deficiency' set out in the pamphlet, 'Social Credit's Solution'. To settle this statistical myth involves an intricate discussion in the technical field of National Income accounting, which lies outside the scope of a work such as this. I can only state that references in recent social credit literature to the 'Year Book', as indicating calculations beyond dispute and question, are nonsensically misleading.

1

IS THERE ENOUGH PURCHASING POWER?

THE BASIS OF SOCIAL CREDIT REFORM

The social credit movement is at present an exercise in speculative economic theory. I write 'speculative', because nowhere yet has this theory been put to the test of practical experiment or policy. But proof or disproof of an economic theory, by turning it loose on a community as a political reality, is an extremely risky matter. The physical scientist can try things out in his laboratory, modifying, accepting or rejecting as the experimental results come in to be measured against the theoretical beginnings. Denied these opportunities, the speculative economist must be very, very sure of his grounds before he gives his blessing to proposals for this or that course of action. He must, as it were, speculate on the speculations at great length, and measure the plausibility of the new ideas against the untidy world of reality.

The economic proposals of the social crediters, therefore, warrant the most careful examination before they reach the point of practical policy. If flaws in the reasoning can be revealed before the nation becomes the social credit guinea pig, disruption, tragedy and shattered hopes may be prevented.

Fortunately, the social credit proposals concern themselves with only part of the whole economic picture. Social credit theory is usually represented as a monetary theory. It asserts that the money systems of most nations fail to provide sufficient purchasing power to enable the flow of goods produced to be bought. The system underpays itself, with the result that there may be an 'under-consumption' depression, such as we had in the early '30's; or alternatively, buying power can be sustained by injections of bank credit, which keep the wheels turning only at the cost of piling up huge debts. The social credit remedy for this state

of affairs is the judicious provision of interest free bank credit by the State, to balance the flow of goods with purchasing power. This expresses itself in a highly attractive political programme of lowered taxes, higher pensions, interest free government loans, and the like.

But before New Zealand accepts this vision of the promised land of easy money as a realizable heaven, the theory upon which it is based surely deserves rigorous examination and mental effort. The penalty for wrong calculation is heavy: under present full employment conditions nothing short of such an intense inflation that currency values might cease to be meaningful.

The main specific point at issue is the theory of the 'gap', which deals with this question of insufficient purchasing power. This is well recognized by social crediters. Mr W. B. Owen, in his book*, *How Social Credit Works*, refers to the gap in these words: 'The whole argument for Social Credit as an effective reform rests on the proof of this disparity. If it fails, the case for Social Credit fails, and that is why all orthodox economists do their utmost to disprove the analysis of Douglas and to try and prove that purchasing power and prices are equal.'

Here, then, Mr Owen and I agree on the vital central issue: the validity of social credit's standing or falling by its ability to *prove* its theory of the mechanism of production and consumption, operating with a bank credit system, to generate insufficient purchasing power.

And it is my firm opinion that the theory of social credit in this regard is demonstrably false; that translated into policy it would produce an almost immediate economic crisis of inflation, and that most of the more general arguments supporting this thesis are fatuously optimistic, deficient in historical perception, and philosophically unsound. These are strong criticisms; I hope I may be able to show that they are not unjustified.

THE 'A' PLUS 'B' THEOREM

The theory that purchasing power must *always* be insufficient to buy the goods produced originated in the work of C. H. Douglas. He separated the costs of production into two types: the 'A' payments consisting of amounts going to individuals,

* References to Mr Owen are hereafter quoted from this work.

and 'B' payments, amounts going to other organisations. 'A' payments include wages, salaries and dividends. 'B' payments, to external organisations, include raw materials, interest, etc. The distinction is far from clear: is a private landlord who gets rent for a house an 'A' receiver (as an individual) or is he an 'external' institution? But I shall come back to this point later on.

The Douglas argument now runs on: *costs* must include the 'A' items plus the 'B' items—all are charged in. But *incomes*, the wherewithal to buy the goods produced, are merely the sum of the 'A' items. The 'B' payments are costs which are not available as purchasing power: this is the gap which maladjusts the economy. A simple example may make this clearer; Mr Owen has set out something very similar in his book.

'A' PAYMENTS	Wages, etc ...	£100	Available as purchasing power.
	Dividends ...	£10	
'B' PAYMENTS	Raw materials ...	£30	Not available as purchasing power.
	Interest, etc. ...	£20	
Total costs ('A' + 'B')		£160	
Purchasing power ('A' only)		£110	
'Gap'		£50	

This apparently shows £110 in incomes, trying to buy goods priced up at £160. Here is the gap to be filled. In words quoted by Mr Owen, 'Since "A" will not purchase "A" plus "B", a proportion of the product at least equivalent to "B" must be distributed in the form of purchasing power which is not comprised in the description grouped under "A".'

As it stands, the argument does not convince. Surely, it may be pointed out, the 'B' payments must *ultimately* find their way into consumers' pockets. What about the wage payments of the manufacturers of raw materials? What about salaries and dividends paid out of bank interest receipts? More explanation is needed, and a more complicated example must be introduced to show production as a chain of processes. There is a tradition of using the making of bread for this purpose, and I shall honour it. My example is intended as an illustration; the fact that the figures and times are hardly plausible is not here to the point.

The emergence of a loaf of bread on to the shelf of a grocer's shop is the final step in a chain of production which may go back a very long way, perhaps to the building of an oven, or the draining of a paddock, in Victoria's days. But I shall take up a study of this imaginary chain at three final stages which are supposed to be one year apart.

In 1952: a wheatgrower produces wheat at a cost of £1,000.

In 1953: a miller grinds this wheat into flour, adding value to it of £250, making the cumulative cost of the flour £1,250.

In 1954: This flour is baked into bread at an additional cost of £500, making an output which costs £1,750 in all.

This situation may now be set out in terms of 'A' and 'B' payments and costs. The arrangement is simplified if all the expenses of 'adding value' at each stage, such as the farmer's wage bills, profits etc. are considered as 'A' payments. The cost of the raw material purchased from an earlier stage in the production chain is a 'B' payment. Thus:

	£
WHEATGROWER, 1952—	
'B' Payment (fertilizer, etc.)	400
Plus 'A' Payments (added value), for wages, profits, interest, etc.	600
MILLER, 1953—	
'B' Payment (for wheat)	1,000
Plus 'A' Payments (added value), for wages, profits, interest, etc.	250
BAKER, 1954—	
'B' Payment (for flour)	1,250
Plus 'A' Payment (added value), as before	500
	£1,750

It will be noted that the 'A' payments of one business, passing through the production chain, become part of the next firm's 'B' payments. Furthermore, as set out here, the Douglas gap is £1,250, the sum of the pre 1954 'A's' added up into 'B's'. The 1954 'A' payments are only £500; not less than £1,750 has been costed on into prices. And I should like to suggest that the important distinction between 'A 'and 'B' payments is not their receipt by individuals or external organisations, a difference which gives rise to difficulties, as I have already pointed out, but

a time distinction. This would view 'B' payments as covering 'A' payments made in the past.

Mr Owen appears to admit that this time-distinction is at the heart of the matter. I will quote him quite fully on this, because it is at this point that the falsity of the Douglas theory can be demonstrated. Mr Owen writes (of an analysis very similar in outline to the one presented here)—If all these disbursements were saved and made available at one particular moment of time the bread could have all been sold.'

'But they were not all saved and they were not all available. Link needed: A period of three years has elapsed since the first disbursements were made and most of them were spent and no longer exist. This is true right through the series. The mill cannot grind with water that has passed.'

Again, he quotes from H.M.M. with approval, who writes, in part: 'All "B" items in cost were once "A" items if we go back far enough, but money earned in the past is spent in the past and no longer exists.'

Up to this point I have jogged along more or less with Mr Owen, setting out the theory of the gap much as he does, with some minor changes and simplifications. I have deliberately left the question of savings aside, but only for the meantime. Now we come to the parting of the ways.

Let us assume that this section of production we have studied is part of an established industry running continuously. Wheat-growing, milling and baking all produce at the same time, as of course actually does happen. Further, assume that there are no changes in prices and costs for the term of this study.

Suddenly the 'series' picture, with its notable gap of purchasing power, is transformed. The gap, in fact, completely disappears. Consider closely the following representation:

DATE: 1954

WHEATGROWER	MILLER	BAKER
'B' £600 + 'A' £400	'B' £1,000 + 'A' £250	'B' £1,250 + 'A' £500
= Wheat worth £1000	=Flour worth £1250	=Bread worth £1750
To be milled in 1955 & baked in 1956	To be baked in 1955 (it is 1953 wheat)	Baked from wheat grown in 1952 & milled in 1953

In this continuous flow of production (the device of the years 1952-3-4 is clearly artificial) an individual unit of wheat takes time

to move through the chain, for obvious physical reasons. *But the payment process is simultaneous as set out here.*

As long as the system runs steadily, the 'A' payments will match the value of the goods produced. We get, at any given time:

The Wheatgrower's 'B' Payments (if broken up they become 'A' payments for others back along the chain)	£600
The Wheatgrower's Own 'A' Payments	£400
The Miller's Own 'A' Payments	£250
The Baker's Own 'A' Payments	£500
	£1,750

The realism of this simultaneous view of production should be apparent enough. As I write this, the wheat for future consumption is growing in Canterbury and the farmer is paying his 'A' payments, that is, simply his current outgoings. The mills also are grinding, and the miller pays his way. Bread appears daily in the grocers' shops; all the 'A' payments of the chain are available to buy it and other things. There is a flow of incomes and a flow of bread production. True, the 7d the miller pushes across the counter for his particular loaf of bread may have been earned for producing flour which will be baked at a later date. But if the rates of output are not disturbed, and if plant capacity throughout is not changed, the system is in balance.

All this may be represented in the clearest way (omitting all detail for simplicity) as follows:

THE DOUGLAS PICTURE OF THE GAP

Year		'B'		
1952	.....	WHEAT	Flour	Bread
			'B'	
1953	.....	Wheat	FLOUR	Bread
1954	.....	Wheat	Flour	BREAD

The raw material moves along the underlined path.
Payments for the underlined wheat and flour are lost—not available to buy 1954 bread.

But while the raw materials flow from year to year the income-payment process is simultaneous, as shown opposite:

THE DISAPPEARING GAP

Year		← Income/Payments Flow →		
1952	.....	*WHEAT* ('A') +	FLOUR ('A') +	BREAD ('A')
1953	.....	WHEAT	*FLOUR*	BREAD
1954	.....	WHEAT	FLOUR	*BREAD*

The raw material still flows along the path indicated by the italic letters. The income-payments flow, however, is horizontal; there is no Douglas 'gap'. The 'B' payments are part of the 'A' payments of previous years in this continuous system.

GOOD TIMES AND BAD: THE INVESTMENT PROCESS

It is a commonplace of practical observation that economies do not habitually run in balance, in the sense that purchasing power is able to take off the market just that right flow of goods and services which will keep things spinning along on an even keel. Sometimes the system seems to over-reach itself; goods become scarce, prices rise, and there are more jobs about than there are people to fill them. These conditions—call them boom, or inflationary, or refer to them as a state of over-employment—are familiar enough to New Zealanders. For the last decade we have experienced them; prosperity has been our measure, but with the frustrations and irritations of rising prices and shortages to mar the serenity of the situation.

It is scarcely in accord with practical common sense that recent economic troubles in this country should be ascribed to shortage of purchasing power. On the contrary, surely a more reasonable interpretation is that buying power has been too strong, that demands have fallen so heavily upon our ability to produce and export that efficiency has often suffered, and equitable distribution of scarce goods proved difficult to attain.

It should be noted, too, that a situation where purchasing power is generally strong does not necessarily mean that this, that, or the other line of goods will be in demand. Individual markets have their ups and downs, as the competitive process of business, the vagaries of public taste, the availability of substitutes, and other conditions may bear upon them. An inability to sell a large line of toy trumpets need not indicate a shortage of purchasing power as a whole. Nor should the sight of well stocked shelves in shops be regarded as a sign of too many goods. The best indications of upswings and downswings are falling prices and widespread unemployment for the process of depression, and

rising prices combined with a shortage of labour and materials for the boom.

In common with most other countries, New Zealand can look back past the inflationary period of the 40's and 50's to the slump of the early 30's. Here is a mystery which preoccupies ordinary citizens, politicians and economists alike. The tendency for economic conditions to swing up and then down again, the fact that trade moves in cycles, is deeply disturbing, when what most people want is stability at a prosperous level. Can this be explained?

I am led to this because, in refuting the social credit gap, I portrayed a simple example which was in balance, that is where purchasing power was at the right level just to take up what was coming on to the market. But the trade cycle of reality suggests that the whole story has not been told. Under-consumption is possible, and so, too, is over-consumption, which is one way of describing a condition of too much demand.

The way to understanding how these swings may occur lies in an investigation of two perfectly familiar economic processes, investing and saving. Each must be treated in some detail, so saving will be left for the next section. Meantime, investing may be looked at on terms of the little model of bread making. And I should make it clear that I am not here using the term 'investing' as referring to a purely financial process of borrowing money, or buying shares, or taking over a mortgage, or the like. I am using it in the special sense of actual physical use of resources devoted to building new 'capital' goods.

Now for the model. Suppose an expanding society requires more bread, which may be imagined as coming from more wheat, a new mill, and new bakeries. Capital expenditure is involved, and these outgoings will be made *before* the production of consumers' goods can be increased.

Starting off on an even keel we have:

Year				
1953	.....	Wheat	Flour	Bread
1954	.....	Wheat	Flour	Bread

At this point imagine a simultaneous expansion in 1955, giving:

1955	.....	Wheat	Flour	Bread
		+ Capital expenditure for more wheat	+ Construction costs on a new mill	+ Building new bakeries

Capital developments involve payments for raw materials, labour, etc., in the usual way. These payments are spent on consumers' goods. In commodity terms, the men working on the new mill and the rest are consuming their beer and bread like everybody else. But *for the period of construction,* they produce nothing useable by society; they add not one jot to the flow of goods and services society draws from. We get, then:

1955 ..... Wheatgrowing + Flourmilling + Breadbaking
(Creating the normal purchasing power to buy the bread.)

PLUS Capital expenditure on expanding wheat production, flourmilling and baking, generating extra purchasing power for the limited quantity of bread produced.

A more spectacular illustration of this process comes from the State Hydro Scheme at Roxburgh. The expenditure there has in past years run to some millions of pounds. A young town of workers and their families is consuming food, clothing and the usual things, just as the rest of us do. What have these workers produced to add to the pool of goods and services from which they have drawn so heavily? So far, nothing at all. Is not, therefore, this sort of demand inflationary, in that purchasing power is generated before the goods to offset this come on to the market?

As set out here, investment *is* inflationary. It represents a sharing of currently available consumer goods and services with workers who, *in the short run,* produce nothing. The abstinences involved in this investing process, will, in due course of time, be rewarded when the new project, whatever it may be, is completed. It is interesting to contrast in this respect the wealthier nations, who can spare the resources for capital workers, with the poorer ones, who can hardly turn aside from the immediate problem of getting the bare necessities to live on, to store for the future through capital construction.

Investing, therefore, gives us a first genuine qualification to the original balanced economy presented here. An expansion of the resources of the system, i.e., an investment programme embarked upon will, other things being equal, release extra purchasing power to bid for consumers' goods available. This could be inflationary, causing higher prices and scarcity.

But there is an offsetting item to take into account, as will appear in the next section.

GOOD TIMES AND BAD: SAVING

It has been shown that production generates incomes which can then be used to consume, to take up the things produced. But incomes can be received without this necessarily leading to the second step of consumption. The custom of saving is widespread, and it must clearly affect the rate of consumption at any particular time. Imagine, for a moment, what would happen if all the consumers in New Zealand were suddenly to start saving as hard as they could, cutting down their living standard to the most meagre possible. It requires little imagination to picture the throttling of trade which would result; an under-consumption situation would quickly announce itself with falling prices and growing unemployment. Similarly, of course, a universal flurry of extravagance, in which people liquidate savings they already hold, could push us into a scramble for goods, and rising prices.

Of course, these things do not happen in the ordinary way. Habits of saving are, fortunately, among the steadiest and most sober of the economic virtues. Many people contract to save by means of insurance schemes, superannuation and the like. Businesses make setting aside reserves, depreciation allowances, and so on, a matter of settled and steady policy. And there is, too, a large amount of saving, from which there is no escape, in the necessary thrifts which have to be exercised to pay off debts, such as we commonly see, for example, with table mortgages and hire purchase repayment agreements.

The best general way to look at saving is to regard it as a renunciation of the right to draw from the communal pool of goods and services available. Abstinence may be voluntary, or it may be compulsory. And the savers may have very different ends in view. Many store up their resources vaguely enough with reference to rainy days to come. Some take a long view to their heirs and assigns. Others may hold back for a blow-out at Christmas, or a holiday abroad. Businesses may have definite objects for their saving: depreciation allowances to meet the cost of plant replacements, ploughed back profits for new plant somewhere in the future, and less specific parsimonies.

In some cases, too, saving represents a funding of current earnings to yield a secondary income, through interest receipts, which is additional to, and not dependent upon, day to day efforts.

General matters about interest will come up for attention later on; it is enough to mention here that savings have an economic worth, measured as interest, which greatly affects the motive to accumulate. Life insurance and superannuation, for example, could not run as at present without interest. It is not denied, however, that many people would save even if no interest were received, or that much saving is relatively unaffected by moderate changes in interest rates.

Most people consume only part of their incomes as a regular thing; the balance is saved, either as an accumulation of assets, or a repayment of debts. This is commonplace enough. Unfortunately, from the economist's point of view the matter does not rest there. The importance of saving should already be manifest. It sets the level of effective demand for goods and services; as it changes, other things being equal, so will the level of the public's expenditure. The rate of activity of the whole economy, with its possibilities for booming or stagnating, is brought into the picture.

It is a pity, therefore, that more is not known about what makes people save; indeed, private saving is not even easy to measure statistically. It is usually assumed that as people become wealthier they save a greater *proportion* of their incomes. It is also thought likely that a time of falling prices and threatening unemployment will induce people to try to save more, whereas a boom with rising prices will open their purse-strings, as goods become relatively more attractive to hold than money.

But there is an element of conjecture about general statements on savings, which seems as inevitable as it is unfortunate. For, as many readers may by now be starting to suspect, it is on the interactions of savings on the one hand with investments on the other that the balance of the economy rests.

GOOD TIMES AND BAD: HOW THEY COME ABOUT

We may now consider saving and investing in a very general way, which will greatly help in understanding the question of what keeps an economy running at this or that particular level of prosperity. *Investing* is a process of production, backed by demand, which takes out of the flow of goods and services without putting in. It is an overdraft upon the present for the productivity of

the future. It must be carried as a burden upon output capacity at any one time. It has a financial side (which will receive attention later), and it has a real side in terms of physical things.

Saving is a kind of counterpart to investing. It represents a process whereby more is put into the flow of goods and services than is taken out. It, too, has a financial side, as well as a physical side of abstinence.

And now we can pull the rabbit out of the hat. If a community saves more than it invests, there will not be enough effective demand to take up the goods produced, and the system must tend to contract by the usual unpleasant means of unemployment and price falls.

If, on the other hand, investing proceeds at a faster rate than saving, the overdrawing side of things more than compensates for the saving, or holding back. This is the case of boom, when effective demand presses so strongly upon current output that capacity becomes fully employed, and prices have to rise. The rate of activity of an economy is a result of the interaction of these two counteracting processes, saving and investment.

Contrast this explanation with what social crediters assert. Their fallacious theory of the 'gap' leads them to proclaim a permanent shortage of purchasing power. *Never* can the goods be taken up; *never* can effective demand match supply. One might expect, therefore, that economies would shrink, and go on shrinking in these unhappy conditions. And so the social crediter is forced, because of the implausibility of the conclusion his theory of the 'gap' forces him to, to bring in the money system to solve the question of how an economy can work at all, with the 'gap' in constant attendance. The banks are then pictured as filling this 'gap' to their own private gain. How extraordinary, therefore, that banks should be so vilified in social credit literature; private gain or no private gain, we should have shrunken up to nothing without them, if we believe social credit. And so, if filling the gap is not anti-social, one final thing must be made so—the bank charge for its services. The ultimate villain is the rate of interest.

What I have here written contains an important point, apparently not noticed by social crediters. Suppose, for the moment, we admit a state of affairs where effective demand is too weak to sustain production because of the 'gap'. And suppose the banks fail to oblige with appropriate villainy in pumping in more paper demand. The process of shrinkage would surely be cumulative.

As people become unemployed, their production is lost; demand is *always* less than current production, so things must go on down and down. Surely an unfilled gap in demand would not stop short of complete breakdown. For *never* is there any let up with the 'gap'. And if increasing debts and bank credits are the only remedies for the unenlightened, it would never be possible to reduce either of these without a disastrous shrinkage in total demand. How, then, do social crediters account for the apparently successful reduction of debt in Alberta, which does not practise social credit?

What actually happens, of course, is that our economic affairs have shown a marked tendency to ebb and flow. We seem to suffer from too little, or too much. And a general explanation for this lies in what has already been examined, the push-pull of savings and investments.

Although this explanation is illuminating, I want to be careful not to let it say too much. The operations of these forces to invest and save are extremely complex; in certain circumstances, too, rapid swings may occur. It is far from true to suggest that knowledge of these phenomena provides a sure and safe base for political policy to follow. Nothing in what I have so far written should be interpreted as implying that anti-slump or anti-inflation policies are just a matter of encouraging savings, or pump-priming investment, or something like that.

One very serious difficulty concerns the self-generating nature of an economic swing to or away from prosperity. Consider a position of threatened slump. Prices fall, unemployment is growing, stocks are accumulating unsold, and actual production is shrinking. The situation is all in favour of more saving; some of this indeed, is involuntary—the accumulation of unsold stocks. The private consumer will save more, if he can, for two reasons: falling prices suggest that he will be able to get more for his money next month or next year, and he is likely to be scared of the insecure situation, reacting by holding on to his liquid resources as hard as he can. Further, if he is paying off debts, i.e., saving to meet past overdrafts on the community, falling prices will make the 'real' cost of these heavier—he is thus forced to save more in this respect, just as the business man is forced by his stocks to accumulate. And savings, we already know, weaken effective demand unless they are offset by investment.

It would be a happier world for us all if investment would expand more or less automatically as savings contract. But this is, unfortunately, far from the case. Depressed business conditions are not a time for buoyant investment; falling prices again lead to a postponement of operations, to catch lower costs this year or next; lower sales hardly encourage installing new plant, and it is as hard to find a reason for borrowing as it is to find a willing lender, in risky times. And so heavy savings (relatively) combine with falling investment to shrink up total demand and economic activity as a whole. Once the ball gets rolling in this direction it can keep going with its own momentum. It will hit rock bottom only at some rather indeterminate point where prices stick (perhaps as a result of a stand by Trades Unions), the community can no longer save any more, and investment just has to pick up a little as plant wears out.

A similar general picture may be drawn of a boom economy. Here, rising prices scarcely encourage saving; buy now, it will cost more next month for the same thing. And with jobs easy to get, lavish spending seems reasonable, and in accord with the spirit of the times. So the private consumer may easily become an investor, by signing up for a car, a refrigerator, or a new house—taking out of the pool more than he puts in for the time being. And business, too, spurred on by easy markets, puts in new plant and replaces old. Savings low, investment high, and up goes the balloon of inflation.

It is useful to grasp a general explanation of this sort in order to understand how prosperity comes and goes. But there is too much facility in my generalizations. It is all very well to write about savings and investments as the touchstones of our economic well-being. The real points at issue for policy, however, are more elusive. More knowledge is needed about what makes people save and what makes people invest. At what point in a changing world are new decisions made? What about the psychological forces which work on us all in boom times and in bad? What part can Governments play in all this? How about such things as population growth, defence programmes, international trade and prices, new inventions, and changing social philosophies, such as we associate, say, with the Welfare State? The saving and investment technique is a fruitful way of classifying a hotch-potch of forces which operate in a modern economy. But reality is still a sadly confused picture, and only some of the

points raised above can be answered within the limited scope of this work. In particular, the New Zealand situation holds matters of special interest, which require further examination.

GOOD TIMES AND BAD IN NEW ZEALAND

Up to a point, what has been set out above gives a reasonable explanation of what has happened in New Zealand. The buoyancy of the post-war years, for example, certainly reflects heavy investment by business and government, combined with a high level of personal consumption of durables, as well as day-to-day commodities. As I write this, at the end of 1954, it is probably true to say that New Zealand's most serious economic problem is to find the savings needed to balance the heavy investment on roads, houses, schools, power schemes, transport, public utilities and all the rest of the capital facilities we need in our rapidly growing community. If savings are not forthcoming, the excess demand which results from the country's trying to overdraw on itself will push us further along the road of inflation. Rising prices, looked at in this light, are the way savings are squeezed out of us, if we do not make them by other means.

Nevertheless, this picture is not complete; the position in this country is complicated by the importance of our export business as primary producers. Two main conditions here make for good or bad times: first, the prices our primary products fetch, particularly in Britain, in relation to the general price level of what we import. And secondly, the relation of these two price systems to internal costs in New Zealand, and to land values.

Any programme which aims to keep this economy away from economic doldrums, such as it got into in the early 30's, must take account not only of the local savings-investment situation, but of the farm income situation. This work is not intended as an examination of such problems, but some general observations may be of value.

It should be noted that there is little reason to hope that a self-adjusting process of markets will automatically bring about stability and full employment (a question-begging, but useful descriptive term) together with incentives for maximum efficiency (more question begging). The economy, as indicated previously, is likely to swing itself up, and swing itself down, on both legs of

the journey moving past the point of desirable stability. Or it may stay up at too high a level for some time; or, of course, remain sunk in depression for too long. Neither the theory of activity and employment, nor the evidence of history, gives us any reason to rely on the old fashioned belief that everything would come out all right, if only business and people were left alone to go about their affairs.

But if Government intervention is necessary to keep economic progress reasonably steady, as I believe it is, there is still plenty of room for differences of opinion, different social and moral values, and different shades of political colour to find their places. Neither the economic theory involved, nor any other attribute of the whole situation, throws us upon the mercies of a single dogmatic view that the *only way* is such and such. Even the confines of the Welfare State leave room enough for the larger social and economic questions to be open ones. Remedies for slumps and booms are still, to a large extent, a matter of what society considers good, and acceptable at the ballot box; it is the faith of democracy that, in the long run, these two qualities are the same.

Perhaps one evident proposition could be still further stressed. If economic activity has its ups and downs, economic policy must change its methods, as it appears that the accelerator or the brake is the more appropriate. What is good policy when a depression reigns, may easily be crass folly in more generous times. To expect a perfectly rigid attitude from politicians about what they shall do now, next year, and next decade, is to confuse folly with consistency. Electors should fully realise that opportunist techniques may be the best political response as prosperity ebbs and flows. We must never accept as 'high minded adherence to principles' a dogmatic obtuseness which refuses to see beyond the end of its nose for fear of having to change its mind. Judge, then, social credit, with its simple theoretical belief in a single (and erroneous) idea, its foot pressed firmly on the accelerator to speed us over a 'gap' that is not there, come boom, come slump, come anything.

Questions Asked and Answered

1 *Is there any denial here that a 'gap', a deficiency in the purchasing power necessary to sustain full employment, may sometimes exist?*

No. It is argued that economic activity ebbs and flows. In the depression, for example, there was a deficiency in purchasing power.

2 *Are you really explaining, then, that social credit theory is right for part of the time, for the periods of depression?*

No. The Douglas analysis of the gap is a wrong interpretation of how the system works, and the fact that a 'gap' may exist at times, merely makes social credit occasionally right for the wrong reasons.

3 *Nevertheless, would not a social credit 'dividend' have helped us in the blackest days of the slump?*

It would have stimulated our moribund economy, although perhaps only temporarily. But as a technique for lifting effective demand it is crude, and full of risks for letting prices get right out of control. A variety of better methods is available within the framework of more normal political action.

4 *Is saving a bad thing to do when a slump threatens?*

For society as a whole, yes, especially if such savings reflect the tightness of bad times. Demands which would help to keep things going are held back. But for one person and his family saving may be both wise and prudent. Here is a case where private and social interests are not the same.

5 *I have held £1,000 in the Savings Bank for the past few years. Am I saving in the sense used in this work?*

No. The £1,000 represents past saving. You are an active saver only insofar as you are currently putting in more than you take out.

6 *Suppose I lend the £1,000 to somebody to build a shop. Is that investment in your sense, even when the savings have already been made?*

Yes. Building the shop represents taking out more than is put in. It may be fifty years or more before that shop has finished putting in, i.e., is worn out. No matter how financed, the building of that shop is investment, as here defined.

7 *One can see capital goods in course of construction. Is there any physical counterpart to fit savings, or must these be merely represented by money?*

Abstinence, in the sense of not consuming all we might, is not a good physical measure of savings. To a slight extent an economy can save by piling up unused stocks in warehouses. But its ability to do this is very limited. The process of production and consumption is continuous, and can easily be choked off. Recall how quickly Britain's recent wharf strike piled up goods which became an embarrassment. If commodities cannot move quickly into consumption, production has to be checked, which means unemployment. Oddly enough, the physical counterparts of savings are exactly the same as of investment. The only way a system can store things up, physically, apart from the limited stocks already mentioned, is by putting resources into capital goods. And so it turns out that, from this point of view, savings and investment are the same thing.

8 *Do depreciation reserves cause special difficulty? These reserves are charged as costs. But it may be years before they are spent.*

These reserves are saving like any other. They will create a 'gap' only if investment does not take up the slack. In terms put forward to answer the previous question, a business cannot store up physically to replace its machines. It can hold money, which is not the same thing. But it *can* take over all or part of an investment as a means of storing, e.g., it can build a shop for later re-sale when it needs its machines. Or it can lend its savings to somebody else to invest, which is the everyday common sense of the matter. If nobody wants to invest, such storage becomes impossible, and the system then shrinks because of the insufficiency of purchasing power.

9 *Is it true, then, that unless savings are invested as they are made, they may be lost?*

Yes, in the sense that production lost through under employment of resources can never be recovered. But remember that the money titles resulting from the savings will still exist, and can be used for investment at any time; the abstract claim can be made a real one on the flow of goods and services.

10 *Is not social credit a money theory? Why, therefore, does not money take a larger place in the text?*

Patience. Read right on, because Part II is about money. Whether social credit is, however, a monetary theory is arguable, as will be seen.

2

MONEY AND BANKING

A WORKING MODEL

The importance of money, as a real or symbolic force in people's lives, is a theme unduly neglected in fiction since the novelists discovered sex; be that as it may, the economics of money are to most a mystery about which, when they think of it at all, people are inclined to be suspicious and sceptical. Perhaps this arises from the fact that the institutions through which money operates have grown into their present forms as a result of trial and error. And the administration of money is still decidedly an Art. I suppose, in this Age of Science, I should explain that this is not a criticism.

To give a simple outline of how money works, and is controlled, is far from easy in a short work like this; necessity drives me once again into a small imaginary world to illustrate the main points. Suppose we people this one with a small trading community, with no exports or imports to complicate matters, and, at the wave of a wand, possessed of a fixed number of gold coins used for money. The coins move to and fro as economic activity dictates. One interesting point is at once obvious: the supply of money is fixed. It is not destroyed or created by being spent. Business may be brisk or slack; prices may rise or fall (i.e., the value of the gold coins in terms of goods may rise or fall) but the quantity of money is unchanged. Spending it does not destroy it: *the significant fact is the number of times the coins change hands.*

Now add to this community a man we shall call the Banker: his first concern is probably to provide safe storage for his customers' gold, but his business grows, as we shall see. Depositors receive from him a paper receipt, to show they have placed so much gold with him. And it would not take long for depositors to discover that paying a debt may be done very conveniently by

simply handing across a receipt of the appropriate value, leaving the gold in safe storage. Such receipts are a type of banknotes; in a generally acceptable form they would not be unlike our present day cash; as written orders they resemble cheques.

Our monetary world is still essentially unchanged; all that has happened so far is that the use of a more convenient paper substitute for gold has started. But, at this point, an important innovation may emerge. The Banker will find that his business can extend beyond mere safekeeping. People want to borrow money for various reasons, and, as the repository of stores of gold, the Banker will find himself pressed for loans, on which earnings in the form of interest can be made. Not only this; the Banker does not always need to hand out actual gold—his paper promises to pay are acceptable, and will usually serve equally well.

Here the really important development emerges; the gold becomes a 'cash reserve', used as a base on which a structure of paper credit may be built. The supply of money is no longer fixed; it can vary with the demands of the community for money, and the supply of credits issued by the Banker. Of course, if all the paper notes were presented to the Banker simultaneously for gold, he could not meet the 'run'. Normally, however, this will not happen. But a proportion of credit issued will always be wanted in gold, and this, in fact, sets a limit to the Banker's paper issue.

Note further that the community regards the paper receipts as money. Individuals hold them as assets. But to the Banker they are a liability, a record that he may be asked to pay the holder a certain amount of gold. The Banker certainly creates credit by his paper issue, *but it is not his own credit.* His profit comes from the interest, or service charge on loans. He does not create money for himself, but for others. And so the Banker's 'paper' shows as a liability to him. In an issue of paper fully backed by gold the simplified picture the Banker's Balance Sheet is:

LIABILITIES	ASSETS
£1,000 worth of paper receipts issued	£1,000 (gold coins)

Assume that the Banker estimates that he can issue excess paper above his gold holding to the extent that a 10% cash

reserve will be a safe position. We have then:

LIABILITIES	ASSETS
£10,000 issued paper receipts	£1,000 gold coins
	£9,000 loans
£10,000	£10,000

The amount of paper that the gold can bear is a variable figure, which will depend upon all sorts of conditions in detail. But one basic point must be clear. Without the *confidence* of depositors, the Banker could not operate as a 'house of issue' at all. Once confidence is established, other limitations come into play to restrain the Banker's hand.

There is first the condition of creditworthiness in the borrower. This party must have a worthwhile project in mind: also security of a more or less tangible nature, to constitute an asset to support the Banker's liability. And he must offer reasonably good prospects of prompt repayment. The Banker dare not get his resources laid out in unrealizable assets; liquidity must remain a prime aim with him. All these conditions are more restrictive than might be supposed. Far from being able to create credit out of nothing, the Banker can usually only assume limited demand liabilities (that is, issue loans) when these finance a fairly narrow class of transactions.

And, as already mentioned, the second limitation is that of the Banker's cash reserve. His business is built on confidence; if he threatens this by rashly issuing paper to unreliable customers, beyond the ability of his gold to meet, he tumbles himself, his depositors, and his profession, into disrepute and ruin. This is not fancy; there is a grim history of actual bank failures to attest both the risks and the limitations.

And now an important question comes up. Is a bank loan inflationary?. Applying the tests set out in earlier pages we may answer as follows: The bank loan permits the borrower to draw more from the pool of goods and services, for the duration of the loan, than he puts in. It is a sort of short term investment. This will be inflationary (if savings remain constant) because it will lead to an increase in effective demand. If the economy is not working at full blast, the extra business may well help to get idle resources back to work. But if the economy is already fully employed, and savings remain unchanged, some

inflation may ensue. This is true of course, only of *increased* loans; the renewal of loans to people out of repaid overdrafts is a self balancing process of issue and replacement, in which the supply of money remains constant. And it follows, of course, that a sudden retraction of bank overdrafts is equivalent to saving, with the threat of falling demand this implies.

Finally, it should be realized that an increase of the Banker's credit is not the only source of investment. The use of any sort of accumulated savings will do the same thing. It is in those investment fields where specifically short term requirements need to be met that bank credit plays the important part.

And now a big jump must be taken from our Banker, in his little world, to reality. An outline of the New Zealand banking structure will make more sense against the background of this model, for the basic principles of banking and credit issue have already been explained. And New Zealand banking organisation works with a family resemblance to the techniques practised abroad.

BANKING IN NEW ZEALAND

The core of our banking, its cash reserve, is our holding of sterling currency. We can ignore a token amount of gold. Most of our sterling is held by the government-owned Reserve Bank. It is a central bank: that is, a kind of wholesaler of credit, dealing directly only with the Government accounts, and with the Trading Banks, the retailers in the business, with whom you and I conduct our affairs.

Remember the rule: a Bank can issue paper which may be regarded as money by the receivers, but is a liability to the Bank itself. The Reserve Bank's paper consists of our actual banknotes and coinage, together with various advances, mainly to the State. Any banknote bears the 'promise to pay' inscription; in the New Zealand case, the phrase means to pay out of the cash reserve, which is sterling. Clearly, with exchange controls and import licensing, this promise has been conditional for many years. It is likely to be nearly met by the time this goes into print. The State, too, strengthens the hand of the Bank, and protects the confidence of stability in the situation, by declaring the Bank's paper 'legal tender', a self explanatory term.

Credit dealings with the public are in the hands of the Trading Banks. *Their* cash reserve is their holding of Reserve Bank money, whether as actual notes and coin, or as deposits, and relatively modest holdings of sterling exchange, for conducting day to day business. And the paper super-structure of the Trading Banks is, of course, the ordinary advances made by overdraft to the New Zealand community.

All this may now be set out in a simple representation as follows:

THE RESERVE BANK OF NEW ZEALAND

Its *money* is sterling currency.

It builds on this, through the various Public Accounts, a superstructure of credits (including banknotes, etc.), which are its liabilities.

The Trading Banks acquire some of these credits by their normal trading. This is their *money*.

They build upon this their structure of deposits and advances. This (together with banknotes and coin) is the public's money. These advances are a liability to the Trading Banks.

Central Banks are often called 'Banks for Bankers' and this is shown clearly above. The Reserve Bank is, by virtue of its position as a 'wholesaler', strategically placed to dominate the issue of credit in New Zealand. By changing the cash reserve requirements of the Trading Banks, the Reserve Bank can tighten or loosen the borrowing facilities the public may use. And there are other means of control.

Perhaps the limitation on issue of credit can be brought home most clearly by two examples. On average, of every £ spent in New Zealand, around 7/- goes on purchases which use up sterling currency. Hence, for every £ of credit created, about one third may be expected to reduce sterling balances. This is the nation's cash reserve. If too much credit is issued that reserve must be eaten away. Some readers will remember that something of this sort happened in the late 1930's, when the use of Reserve Bank credit for State housing helped to reduce our sterling to dangerously low levels. Import controls were the result of this: the Reserve Bank's promise on its notes became

conditional. An 'easy' money policy, that is one of very liberal use of bank credits, threatens our sterling holdings.

And Trading Banks must be careful, too. When they make a new loan, their customers may want some of it in actual bank-notes. This draws down cash reserves. Or customers may want to pay the Government with it, and public accounts are Reserve Bank money, which again may drain out 'Bankers' cash'. All this means that Trading Banks must step warily, if their liabilities are not to reduce their cash reserves below the legal limits.

And now for a few main summary points: New Zealand's money, for ordinary purposes, may be regarded as cash, that is Reserve Bank notes and coin, plus deposits at Trading Banks operated on by cheques. This is a credit superstructure arising from both the Reserve Bank and the Trading Banks. Credit may be increased or contracted depending upon customary, traditional and (at some points) legally enforceable attitudes to cash reserves, and the load of credit they can carry. The structure is flexible: it can feed in more cash for Christmas trade, for example, and tighten up after Income Tax is paid in March. If the country's trade grows, the money side can expand, too: as sterling exchange is the base of the system, the importance of our primary produce exports, both as regards quantity and price, becomes self evident. Seasonal swings in payments and receipts can be met by the ability of money to 'breathe'. And the public may have absolute confidence in the nature of the structure; this sort of thing has evolved from much experience. Banking is not only an art, it is a great art.

BRAKING AND ACCELERATING

I hope it is already plain that it is false to regard the Banks as wielders of limitless economic powers through their ability to create credit. Critics of banks and banking, and they appear to be legion, first exaggerate the economic influence of credit, and then vilify the use made of it. Nothing is too big, or too depraved, to lay at the doorsteps of the sinister back room boys of the world of money: wars, slumps, strikes—the tale of their crimes is endless. The cigar smoking, striped trousered, top hatted figure of the banker or international financier is the lightning conductor on which discharges the energy of wrath and frustration.

Banking has made plenty of mistakes: its history, like that of practically all human institutions, is dotted with follies of one sort or another. And at times, more responsibility and power has fallen into banking hands than has been good for it, or the public at large. But this has not been true in New Zealand, at least in this century.

Banks, after all, are little wiser than the general run of social and political opinion in the environments they operate in. During the calamity of the last slump, banking policy might have done more than it did do. But this is being wise after the event. Government policy and economic doctrine were also unenlightened, *by present day standards*. And, the evolution of economic policy has been in the direction of an increasing subordination of the monetary organisation to the growing power of the State in economic affairs, with the banks' agreement and co-operation. For the wise banker is more acutely aware of the limitations under which he labours than the customer, who regards him as the symbol of limitless wealth and power.

But banking may still play a central part in this all important question of keeping things running on an even keel, at a level of full employment. The concertina action of bank credit should, at least at first sight, be capable of expanding to liven up quiet times, and contracting to hold down inflation. The operation is conceived as working not only through expanding and contracting loans, but through the effects of money changes on the level of prices.

There is an enormous economic literature upon how changed quantities of money will affect the level of prices. In detail there is still controversy, but the broad commonsense of the matter is plain enough. For a given number of transactions, more money will bring about higher prices, and less money lower prices. Extend the supply of money, and prices are likely to rise; contract it, and they will probably fall.

But this does not assert that money *causes* the price change. A vigorous investment programme may be inflationary, as we have seen earlier in this work. Such a programme will almost certainly call on bank credit for an extension. The rise in prices which follows has been caused because people take out more than they put in, i.e., are investing more than saving. The money side of the picture is a *result* of this tendency, not a cause.

Nevertheless, it might be argued, surely the banks could refuse

to issue credit in what they regard as a dangerous situation, and control matters in this way. True enough, they might exercise a restraining effect, although they could not stop people from spending their savings or borrowing from non-banking sources. But it is generally correct to regard the banks as possessing good brakes for holding back inflation; and they are not popular brakes. Consider what public opinion would say in New Zealand if all new private housing were to be made conditional upon, say, a two-thirds cash deposit. This is the sort of thing tight bank credit might bring about. Or imagine the public reaction to a heavy increase in the interest charge for bank loans, which is another way of tightening up. Or picture the indignation of a retail trader refused an overdraft to cover the importation of some goods which he knows he can sell, the decision being based on 'policy', and not the trader's creditworthiness as such.

There are several methods open to a Government which wishes to curb unruly prices. Most of them are unpleasant, because they all must involve stopping considerable numbers of people from drawing as much from the pool as they would like. The restriction of bank credit is one of these means, among such other devices as higher interest rates, increased taxes, import and price controls, wage freezes, lowered guaranteed prices, capital issues controls, and a few more nasty economic medicaments. The choice of what sedatives to choose in order to calm the patient is a political as much as an economic one: it is an open question.

And what about the very different position which arises when the economy is too slack, with prices down and unemployment? An injection of credit is surely just the thing. But the trouble is that, as already explained, creditworthy borrowers do not abound at such times. Credit would benefit the community in larger doses, but it almost certainly cannot be pumped in by the banks acting on their own, if they are to behave responsibly to themselves and their depositors by safeguarding repayments. Only the State can do the job. And, once again, a whole galaxy of measures lies to hand, including public works on a large scale, higher guaranteed farm prices, lower taxes and income tax exemptions for new capital developments, higher basic wages, home building guarantees and the like. Here bank credit expansion is only one aspect of a possible programme, which will be weighted this way or that, according to political considerations.

Banking, therefore, is in a responsible, powerful, but somewhat passive role in the whole matter of guiding the economy. Our money organisations are now constituted so that Government policy can express itself clearly and efficiently through the institutions. The Reserve Bank is owned by the State, as is the principal Trading Bank; the other Trading Banks play the game closely according to the rules. And the art of banking, like that of politics or of economic administration, consists of continuing the flexible use of bank credit, along with the other means mentioned, to meet what society considers as good and necessary ends. And it is up to society to discover that sometimes what it does regard as 'good and necessary' contains certain incompatible elements, which have to be resolved in compromise.

SOCIAL CREDIT AND MONEY

In my opening pages I described social credit as a monetary theory; this is not exactly misleading, but in some ways the money aspect of social credit is subordinate to the basic view of income flows, as set out in the A plus B theorem. Indeed, the inaccuracies of this theorem are compounded by an extraordinary view of the money system and how it works.

The social credit view of money appears to be roughly this: Money is created by the banks, so that a pay out from them is an issue of new money, and a deposit with them is a cancellation of that money. A typical economic transaction consists of drawing cash from a bank (or writing a cheque on an account, substantially the same thing) and paying somebody with it. The receiver then banks what he gets. The money has been created, done its job, and then been destroyed.

Now, imagine that a social credit policy is at work in a community. We have already seen that this policy is shaped by the theory that a gap in purchasing power must be filled by the creation of a social credit dividend. This is to be done by the issue of a monetary credit through a State controlled (although, apparently, not necessarily State-owned) banking system. To follow an imaginary single transaction may be illuminating.

Let us take it that the dividend is in the form of a special monthly pension of £10 to a particular class. The banks are authorized to build up their paper issues to meet this. (We will leave the interest-free aspect aside meantime.) A, an accredited

pensioner, gets his cheque in due course, and a bank's paper issue (a liability) is increased by £10, exactly as would happen if a new overdraft were made in the usual way.

Then A proceeds, shall we say, to spend his cheque with the grocer, who then banks it immediately. All these circumstances meet ideally the social credit theory of money springing into existence out of a bank's books, making a single commodity 'kill', as it were, and going back to ground again in the limbo whence it sprung.

But, in fact, will things work out so smoothly? The grocer's position is very interesting. He still has title to that £10, even if he does deposit it. He can use it again by drawing it out in cash, or by writing a cheque on it. True, he may reduce an overdraft by depositing it, *but that will only be a genuine reduction in the quantity of money if the Bank lowers his overdraft limit by* £10. Unspent money held in a bank, whether a 'genuine' deposit (in the black) or an overdraft (in the red), is exactly the same as a wad of pound notes in someone's wallet, awaiting the signal to move on.

There is no alternative to this reduction of overdraft limit; otherwise the social credit dividends (which are *always* needed, remember) pile up remorselessly, adding to the quantity of money. And this can only mean one thing: a general and very serious inflation. The storekeeper pays his social credit tenner to somebody else, who pays it to somebody else, and so it goes on, diluting the value of existing money.

If the economy is already fully employed, as New Zealand's undoubtedly is at the moment, the mechanism of the social credit dividend is now clear. The 'gift' enables the pensioner to take out of the pool without putting in. This is not of course, the present case with those pensioners whose incomes are transfers from other people through taxes. And superannuitants who draw out their own savings can only 'inflate' the economy if working subscribers to funds pay in less than the retired take out, an unlikely contingency in a growing community.

The social credit dividend, is, however, a form of investment as we have defined it, financed by the highly liquid form of bank credit, that is, an increase in the supply of money. Not only is this inflationary; with full employment it is likely to be really dangerous. And the community as a whole will be no better off. For the inevitable higher prices will squeeze the value of the

dividend out of everybody. The simple logic of the situation is that a fully employed economy is producing as much as it can. When more cannot be got, all that is left is to redistribute the national product, either between consumers' and capital goods, or between one group of consumers and another. In this case the pensioners score at the expense of others.

It is, nevertheless, this odd view of money, as created by production and destroyed by consumption, that arms the social crediters against all threats of inflation and price changes. And if we regard money as a kind of coupon, issued against production, and cancelled by consumption, the social credit view of 'sound' money becomes clear. How can prices rise or fall when the flow of goods is exactly balanced by the flow of tickets issued against that production and cancelled through consumption?

But money is not created or destroyed like this. It is *transferred* by production and consumption. It remains in existence as evidence of a claim by the holder over what is in the pool. A payment merely puts that claim into somebody else's hands. Changes in the quantity of money, through new overdrafts or cancelled overdrafts, are a partial measure of the processes of investing and saving only. Not only, therefore, will the new social credit money raise prices by sheer dilution as it piles up. It will, like all other paper issued, draw upon the cash reserves, both in bank notes and, more important, in sterling. Are social crediters going to be able to match their local paper issue with sterling, so that we can go on taking our 7/- worth of imports per £ spent?

THE ART OF BANKING

In building up the picture of how banking works, I have tried to avoid giving the impression that it is a highly systematic affair, working on cut and dried lines, with penetrating wisdom about how this or that change will affect the economy. On the contrary, I have stressed that it is an art, and that, with the benefit of hindsight, we can pick plenty of holes in past banking practice

The basic reason for this is that there seems no way of knowing what an 'ideal' quantity of money should be. Much depends upon people's habits with regard to money. If, for example, hoarding a mass of banknotes in old tea pots becomes a national habit, more cash may have to be fed in if a shortage is to be

avoided, that is if prices are not to fall. It is interesting to speculate whether the 'hot' cash held by tax evaders has, in fact, made necessary more new note issue in New Zealand than would otherwise have been the case.

Again, the seasonal nature of farm production in this country usually means a heavy demand for liquid credit to carry over the time from payments to receipts. The flow is probably more even in secondary industry, and one would expect lower credit requirements. The long haul from overseas to New Zealand too, means another gap between payments and receipts, with its demand for credit facilities.

A sudden increase in the supply of money, therefore, need not necessarily result in a general price rise. It may merely meet a growing public desire, say, to hoard notes. The important questions are: how many transactions are involved, and how fast does the available money circulate to do them? If money changes hands once a year only, the supply of money will have to be roughly equal to the National Income. If it circulates faster than this, a lesser amount will do. I shall try to show this by yet another imaginary example.

Suppose, for some reason or other, that people come to suspect that serious inflation is in the offing. Feeling that their liquid cash (banknotes or bank deposits) is likely to buy less tomorrow than it does today, they naturally tend to get rid of their money as fast as possible, in exchange for goods. They are, in effect, deciding that it is better to store up their economic resources in goods than in money. And, of course, they will buy freely, quite beyond their day to day needs for ordinary consumption.

Two things will happen. The weight of the cash bids for goods will make itself felt as at an auction, and prices, particularly of the more 'negotiable' non-perishables, must go up. The cash is not destroyed by being spent, it is passed from hand to hand, and becomes rather like a hot potato, too painful to hold. Prices may easily start to soar, particularly as the spendthrift wiseacres start in with 'I told you so' type of talk. The rising velocity of circulation is equivalent to an increase in the quantity of money, with the expected results in higher prices. The banks need do nothing here: passing the cash around fast enough would inflate without assistance from the financial wizards.

Of course, such a situation could be corrected by stern bank restrictions to tighten down on money supply, and by the use of

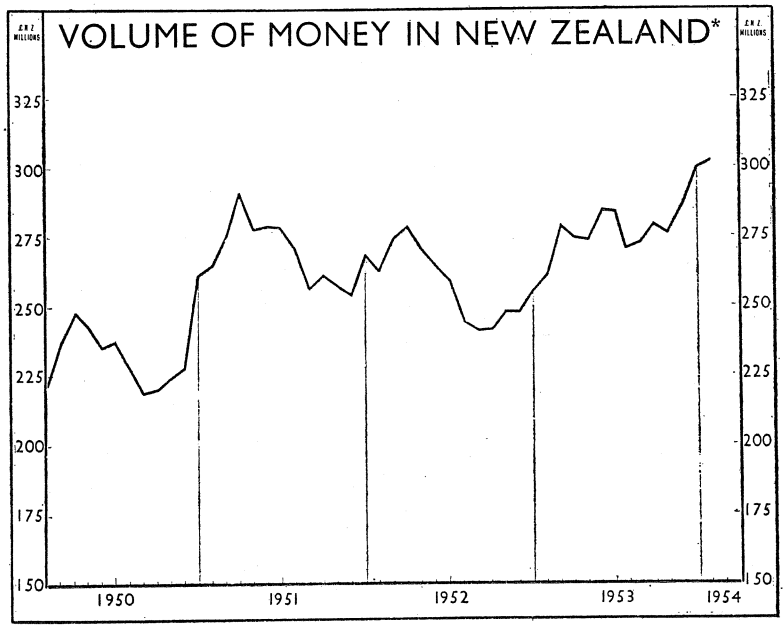
the weight and authority of the State to calm fears. If, in fact, such measures are not applied, a money may lose its value entirely, as prices get right out of hand, and banknotes, with rising face values, find it hard to keep out of the wall-paper class. This is what happened in Germany in 1923. And the ultimate root of such economic and social disasters is a growing convicition on the part of people that their money is not sound as a store of value. Get that idea started, and the situation can very easily run out of control. Could it happen in New Zealand? Of course it could, although it is entirely unlikely unless an inundation of paper credit were to shake public confidence, and start the trouble off. This is exactly what social credit would be likely to do, if given the opportunity to feed in their considerable dividends.

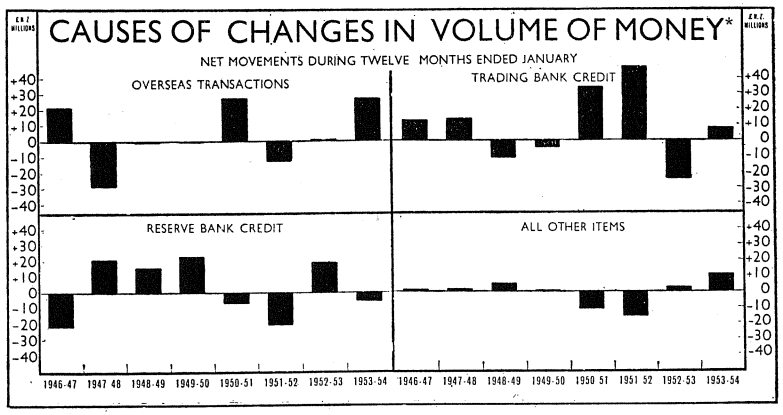
But the expansions and contractions of the money supply, under ordinary circumstances, are the result of people's wishes, or the movement of goods, or of savings habits, or a host of other things. An increased supply of money, for example, such as we may get from bumper wool prices, which feed sterling into our structure, causes no panics or upsets or violent price changes. Even so, the exceptionally heavy lifts, arising out of wool sales a few years ago, were wisely frozen into time deposits, i.e., taken out of the money supply, in order to stop them from pressing too heavily on available goods and services, and pushing up prices. When money works as an *effect* of certain forces the situation is likely to bear up well, but when the idea gets around that the *money itself* is the cause of the trouble—look out!

The general control of money is, because of all these variable factors, heavily dependent upon a sort of month by month sense of the working of the economy. The banker may feel that a money stimulant would put some necessary life into things; he presses his accelerator a little (probably with State support) and suddenly the engine roars into life and goes on speeding up of its own accord. Or he touches the brake for a gentle check, and before he can say 'convertibility', the economy is in a bad skid. As this metaphor indicates, there is no simple mechanical relation between money, prices and prosperity. Money is an important factor in economic policy, but it is by no means the only one. To pin one's hopes of a new and better world upon monetary reform alone is to underestimate the complexity of economic reform as such, and to overestimate the part money can play in it.

FACTS AND FIGURES

The chief facts about the supply of money in recent years are set out in the following graphs prepared by the Reserve Bank of New Zealand.





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The graph line in the upper diagram clearly shows the swings of bank credit due to seasonal factors. In particular, Christmas business followed by the Income Tax payments of the first quarter runs up a characteristic peak each year, which runs down again as the economy recovers its financial wind.

Trading and Reserve Bank credit should need no further comment, but the changes in the volume of money arising out of overseas transactions do not explain themselves. Exports, say of wool to Britain, are paid for in London, and paid out here in New Zealand. The New Zealand money system is extended by an asset (sterling held by the Reserve or Trading Banks) and a liability—the bank deposit made available to the woolgrower. The process reverses itself when importing occurs; in this case we pay out in London, and lose our sterling holding from the Reserve Bank here. The total credit structure here may or may not be reduced, depending upon whether the importer has an overdraft or not. In general the exporting and importing take place roughly simultaneously (there are, of course, seasonal swings) so that the additions and subtractions are self cancelling. An outstanding balance for the year, however, is effectively a change in the supply of money: an export surplus increases the money, and a deficit (excess of imports) reduces it. Both these conditions are subject to certain complications which may occur with Trading Bank credit. This is illustrated by experience in 1951-52 when imports were in heavy excess (which should shrink up money supply), but could not readily be sold locally (which held Trading Bank overdrafts at high figures, keeping up the supply of money).

For the past twenty years or so, both the level of prices and the volume of trade have increased. In this process of growth and expansion, the supply of money has gone up, too. A useful way to measure this is to take the total money supply as a percentage of National Income. In the late 1930's, this ran around 25%. The war proved inflationary, as might be expected, and money supply rose to around 40% of National Income in the late war years. A peak was reached in 1945 at just over 48%, and since then there has been a decline, with ups and downs, to just below 40% in 1952.

It is not easy to read very accurate conclusions into this relative increase in the supply of money in New Zealand since the pre-war period. Cause and effect are inextricably woven together

in the whole history of these years. The young New Zealander, who starts a family on a financial shoe string, borrows for a new house, buys his furniture and durables on time payments, and lands the Government into building a new school place for his children, and various local bodies into sewerage, roading, water and power installations, is as much part of the inflationary scene as the banks, who, to a great extent, have to play along with the self generating buoyancy of these busy times. Inflation is almost a way of life now; this is not to condemn it—in fact, rising prices make for a pleasant enough economic climate, provided they do not rise too fast. But this climate is not set by the banks.

One final fact is patent from the general figures of money supply here quoted. The social credit assertions that the economy has been kept going by injections of debt-accumulating bank credits to fill the 'gap' are not true. The total supply of money in New Zealand has increased by an average of about £16 million a year for the past eight years. This hardly suggests that an enormous social credit gap (of nearly £200 million last year?) is being plugged. And yet the economy is still in a general state of full employment, with production at its limit, and prices edging up. And the Trading Banks, condemned as gigantic hoarders of paper credits, have in some cases gone to the public for increased capital to conduct their businesses. Even if the social credit arguments held a whiff of the truth, one would expect the banks by now to be owning half of the resources in the country. Of, if these paper machinations are Reserve Bank in origin, the State should be (secretly?) possessed of enormous properties; why, then do we hear only of the mounting burden of State *debts*?

Questions Asked and Answered

1 *Do banks create credit?*

Yes.

2 *Do banks create credit out of nothing?*

No. You are reminded of the two main limits explained above: the creditworthiness of borrowers (who must be reasonably solvent and able to repay), and the cash reserve requirements.

3 *But if man can create more money, should he not do so? Shortage of money is the chronic weakness of society.*

Do not mistake the shadow for the substance. If money is not relatively scarce, it will be valueless. A cooling shower of pound notes from the heavens will do me little good, unless it falls in my backyard only.

4 *You argue, then, that monetary institutions work well, and should be left alone?*

Not at all. I make no claim that our knowledge and control of money cannot be improved. But inherent in such improvements are the large and open questions of economic reform—what it shall be, and what policies it shall adopt. Remember that almost any so called change for the better is open to contradiction from an inevitable number who will regard it as a change for the worse.

5 *Would you agree that money, a man-made device, should be always used to give us what we want?*

What are these wants? Remember that the Law, a man-made institution, is devised to prevent many people from getting what they want. Terms such as 'people's wants', 'needs', 'what they deserve', 'better world', and the like, are often ambiguous phrases to conceal special pleading.

6 *You claim that money can be made subject to government policy in New Zealand. Can you show how this works?*

Two techniques will suffice: Our cash reserve is our sterling reserve. This reserve is capable of variation by changing exports or imports. Through such a measure as import licensing, the Government could hoard sterling, and enlarge the basis of our money structure. Similarly, by liberalizing imports, it could shrink it. In each case, money supply could be seriously affected. I hasten to add that no such policy moves have been made, as far as I know; I mention this technique merely to show the power the Government could exercise should it so choose.

Another method is to sell Government securities to the banks or the public. The money used to buy these with can be sucked out of the system by a reduction of the Reserve Bank's paper issue. Buying securities from the public reverses the process, and feeds in more money.

7. *Might we suffer from shortage of money if we had a slump?*

Of course. To a great many people, that is how a slump would appear to hit them. But the shortage of money is an effect, not a

cause. Nevertheless, it would be quite unsound to delay recovery measures because not enough money was available. It is true that money, a good servant, may at times be a bad master, by being regarded as an end in itself.

8 *Are you dodging the difficult question of gold?*

No. It is not strictly relevant for the explanation here. Gold is a traditional cash reserve, which, in some circumstances, may make a credit system behave very inflexibly. Economic policy nowadays usually needs a flexible money system, which makes the use of gold standards, except for countries like the U.S.A. with enormous gold holdings, a matter for debate about whether gold can be made a sufficiently elastic foundation to a money structure or not. And the debate can take on different hues according to opinion, political views, and a number of similarly vague matters, which include crystal gazing.

9 *What would you consider the best practical working rule for administering a money system?*

Avoid rapid changes. Even if an 'ideal' amount of money is anyone's guess (after all, what is an 'ideal' economy?), it is fairly certain that a rapid change from any particular going level, either upwards or downwards, will cause trouble. 'Don't rock the boat', is a maxim as useful for bankers as for politicians.

10 *Will New Zealand's supply of money go on increasing?*

Probably. We are still an 'investment dominated' society, which makes high activity and rising prices a likely type of economic weather for a few years to come. Such an expansion carries its own needs and conditions for further monetary increases. But of course, a severe set-back on the prices we get for our exports could rapidly falsify this view.

11 *Can I find out more about money?*

Of course. A good general book is 'Outline of Money', by G. Crowther. For New Zealand's money affairs the monthly Bulletins of the Reserve Bank are an admirable source: they have articles covering a range of interesting material, as well as a very comprehensive statistical service. The Reserve Bank has also published separately a pamphlet 'Money Supply in New Zealand', which would be invaluable for any who want further information about points touched on here.

3

INTEREST AND DEBT

INTEREST AND PRODUCTIVITY

Most people are superstitious about numbers; most, too, hate economic oppression. Add these together, and the rate of interest, which seems to smack both of a vague and malignant power through the force of numbers, and of cruelly hard economic exploitations of the weak, is scarcely a popular institution.

The vision of accumulating debt, pushed upwards and ever upwards by the merciless logic of the compound interest law, terrifies us as do the echoing concepts of 'infinity' and 'forever'. Little account is taken of the fact, obvious enough to any holder of a table mortgage, that the compound interest law can work two ways, extinguishing as effectively as it accumulates.

The charging of interest on loans has aroused deep and bitter opposition, long expressed by the anti-usury laws which were once a commonplace in Europe. At least two reasons for this attitude may be mentioned: it was usually assumed that an interest contract was fulfilled in grossly unfair bargaining conditions, with the necessitous borrower at his wit's end for succour, and the unscrupulous lender out to wring every penny from his misery. And it was further believed that money, in itself, was infertile; it could not, of itself, sprout a growth which might repay a loan, and interest was therefore, merely, a measure of exploitation.

There were doubtless times and occasions when both these views were justified; there is plenty of historical record of exorbitance in interest charges; we have not been presented with Shylock, or Messrs Dodson and Fogg, for nothing. But in New Zealand today, let him who would maintain that the borrower is still exploited take an open minded look at the conditions, for example, under which housing loans are issued. Or better still, let him consider the present position of landlord versus tenant,

a potent rouser of moral indignation on behalf of the weak in the past.

But of the accusation of the sterility of money, more needs to be said. Money itself may be merely a medium of exchange, a measuring rod for transactions; but what it will buy is perfectly tangible. And the existence of money savings is the accounting side of a real situation: one in which goods and services can be applied to some use other than hand to mouth existence.

This tangible side of storing up has taken various forms: I suppose the pyramids, or the mediaeval cathedrals, fit into place as (among other things) stored wealth. But the modern shape of such activities dates from the Industrial Revolution, when the advances of technology in such fields as manufacture and transport, suddenly offered enormously enlarged opportunities for the productive use of savings.

Consider a simple example: A new railway line may be bored through a hill, giving direct access to a particular place. Or it may be built around the hill much more cheaply, but with higher running costs, because of the greater distance. The tunnel is directly productive: the loan is in no way sterile when used to build it. The savings in cost are directly measurable, and can be applied to an interest payment on the tunnel.

Or, perhaps a laborious hand process of manufacture is made cheaper and quicker by the use of a machine. Once again the productivity of the machine can be estimated, and its earnings applied to an interest payment. In both these examples, correct estimates would include an extra levy for depreciation to turn the compound interest law into its benevolent form.

Behind the facade of money, mortgages, agreements to hire, leases, and so on, lies this very real and important truth. Storing up our wealth is a way to increasing productivity. It is, in fact, the main basis of the important improvements in our standards of living that we associate with technological progress. And interest based on that productivity finds its way into the income stream under all sorts of names—as rents, profits, hire charges and dividends.

But the fact that interest is a payment against the extra productivity a machine or a tunnel may provide, does not enable the debate on interest to be settled out of hand. It is true that productivity is the main justification for interest payment; but it is

also true that 'real' interest does not always find itself well expressed by the 'money' interest rate of any particular time.

Take the case of a farmer paying interest on his land. At the time he took up his farm and arranged his mortgage it may be assumed that his interest payment was considered to be a reasonable expression of the productive capacity of his land. But imagine a drastic fall in the prices the farmer receives for his products. His interest bill does not fall too; it is fixed in terms of a particular historical situation. But a farmer's other costs, and his revenues, change. In this case, the fall in prices raises the burden of the interest charge, and makes it quite unrealistic as a measure of productivity. And, of course, rising prices can lower the 'real' burden of interest, and make a farmer's prosperity as much a matter of the luck of the game as of good farming.

Here we have one objection to interest rates; they are often 'historical'—fixed at a date, and relatively unchanged. Hence, they are greatly affected by price changes, and may lose their 'real' function of measuring productivity. In general, rising prices reduce interest burdens, and falling prices raise them. This latter was a serious matter for New Zealand during the slump; it then gave rise to special legislation. It might be thought, however, that the last decade's rising prices have favoured the debtor; this, in fact, has been so, and makes social credit protests about the growing burden of debt look doubtfully valid on the face of it. But more facts will be given about this later on.

Another difficulty about interest is that it may be greatly influenced by Government policy as a 'money' rate for overdrafts, public loans, and the like. It is not always that the particular 'money' rate will reflect 'real' rates of productivity. For example, the general scarcity of resources for capital development in New Zealand today suggests that a higher rate of interest would help to sort out the stronger from the weaker propositions. But there are all sorts of problems about raising interest rates, many of them political. The result is that interest does not work well as a rationing device to curb our appetites for borrowing. Cheap money is useful for public development: but an inflationary threat lurks here.

Finally, the problems of estimation at times make interest rates rather arbitrary. Even where productivity is a plain issue, as with a railway tunnel, the calculations have to be based on the

future, for the tunnel must be built *before* the revenue can be collected. Future estimates often involve guesswork, and sometimes mistakes are made. Every age produces its 'white elephants', capital goods which are a monument to somebody's over optimism. Further, productivity is hardly a measure suitable to apply as a close check to some forms of public expenditure. What is the productivity of roads, schools, museums, and broadcasting?

HOW INTEREST WORKS

It has often been suggested that interest should be abolished; that this is easier said than done will be plain when the working of interest is looked at in detail. By returning to our railway tunnel, already described in outline above, and putting in some details, the importance of interest will be made clear. Let us suppose that the tunnel will cost £1,000,000. And let us suppose that the net estimated saving on transport running charges, after allowing for tunnel maintenance, etc., will tot up to £75,000. The question is: will £1,000,000 spent now, balance an annual saving of £75,000 stretching into the future?

With an interest rate this problem can be worked out as follows:

		Interest	Saving
At interest 7½%	we get	£75,000	£75,000
,, 5%	,, ...	£50,000	£75,000
,, 2½%	,, ...	£25,000	£75,000
free	,, ...	Nil	£75,000

As there is always an element of guesswork in calculating tunnel costs and operating savings, some margin of safety will be wanted. At 7½% the tunnel is probably not worth building; at 5% it looks a good proposition, and a superb investment at 2½%. Note how the existence of an interest charge enables the problem to be measured up, as it were.

But if interest no longer exists, the problem enters into a new world. The lower the interest rate, the higher the capital cost the tunnel can stand. If the saving of £75,000 set out above is taken as a firm figure, we can capitalize the tunnel as follows:

The Tunnel earns	Interest	Tunnel may carry a cost up to:	Note the compound interest build up of *Capital values* as interest falls. Frightened?
£75,000	10%	£750,000	
,,	7½%	£1,000,000	
,,	5%	£1,500,000	
,,	2½%	£3,000,000	
,,	1%	£7,500,000	
,,	Free	As much as you like to let it. No limit.	

The moral of this example is very clear. A society which proposes doing without interest charges has no market technique for deciding how many resources should go into capital goods. The services of certain productive resources are declared to be 'free'. Imagine what a scramble there would be to get hold of them.

The argument is not upset by stating that the capital must be repaid (without interest). If our tunnel can produce £75,000 of earnings per annum, it can repay *any* capital sum in time. There is still no rationing force at work. Certainly, the problem of the wearing out of capital goods makes calculations of this sort of thing more complicated than in my simple example. But if depreciation is counted in as an operating cost in administering any piece of capital, which is good business practice, the position is still perfectly clear. What is to stop an interest free society from piling almost all its resources into capital goods; from building tunnels, skyscrapers, new roads and power schemes to the exclusion of ordinary bread and butter?

This question is not just rhetorical. There *is* a means of stopping undue expenditure upon capital goods, without interest charges. Somebody must make a decision based upon measures other than costs and revenues. Only one authority can control capital expenditure with a direct 'yea' or 'nay', and that is the Government. An interest-free society is one directly controlled by the State. *There is no way of combining private enterprise with an interest-free society.*

When social credit attacks debts and interest charges, it also attacks the institution of private enterprise. But it supports the latter, apparently very strongly. Here is a fundamental inconsistency which needs further examining: social credit cannot claim the best of two completely incompatible worlds.

Consider first a state of affairs in which no interest charges may be made at all. All productive assets, land, buildings and

machines cannot be charged for. Are private occupiers to reap the benefits of these resources free? And, if so how? How do these resources ever change hands? They can only be capitalized (see the 'tunnel' example above) at infinitely high levels—another way of saying they can never be transferred. In fact, the valuation of all capital resources is stopped in its tracks. There is only one way out of this dilemma: the State must be the sole owner, so that the problems of price and transfer do not arise. This is 'State ownership of the means of production, distribution and exchange'.

But perhaps social crediters will protest that when they attack interest and debt, they do not really mean this sort of thing at all. They might allow that interest and debt are perfectly good institutions for the 'private' section of the economy. They might see the force of allowing landlords, business men, farmers and the rest to value their assets, buy and sell them, and charge for the productivity of what they own. But the State must not do this, they might argue, because the burden of the Public Debt grows intolerable; and the banks must not charge interest, because they deal only in paper.

But a mixed economy, in the sense that one part of it operates without interest, and one part of it with interest, presents formidable problems. Suppose the State uses its undoubted right to issue interest free money to itself, through the Reserve Bank. This is the only way for it to get interest free loans in a 'mixed economy'; the public would lend only to the private section, where it could claim a return. The State then enters into a very one sided competition with the 'paying' section. It can use capital resources without charge; private people pay. Get yourself a State house then: you only pay depreciation for rent. What chance have private builders and owners then? Build plenty of new schools, too. Private industrial building cannot compete when it has to pay its 5%. The Government simply mops up the resources of the country for capital construction at its own will. It must finish by employing everybody and owning everything. Nobody will ever want to do anything privately when State facilities are available at a fraction of the price. Or, if strict rules are laid down to keep the two sections apart, with the Government limiting its claims, not by cost, but by a form of self sacrifice in the public interest, one can imagine the administrative rigidities, and the litigation over awkward border-line cases. One can also imagine the pressures from electors and ratepayers for more magic handouts by the 'free' route. Can our administrative and electoral systems stand this sort of pressure? I think not.

Finally, should banks charge interest? Remember that bank 'paper' still commands the use of resources. If bank credit is to be free, why use any other form? Finance your assets by a bank for nothing. Or if a limit is drawn, who is to enforce it? Is the banker to tell me what I may or may not have, on some vague basis of public interest? or physical priority? or government directive? Once again, we come back to the interest free society as leading inevitably to State control — to Socialism complete.

Social Credit made apparent before the recent election that bank interest charges were to be nearly abolished. And Trading Banks were not to be nationalized. But interest on advances is the main source of a bank's income. And, from the bank's point of view, the interest is reasonable, as an administrative and service charge, for the considerable duties a bank undertakes and renders. Remember, no bank can create its money *for itself*. And note the heavy responsibilities to sustain the rights of depositors and the reasonable certainty of repayment. If a bank is 'infertile' in any sense, then so is any retailer of goods, who adds nothing to what he hands on. The obvious arguments against that view of retailing can be used against criticism that a Trading Bank creates out of nothing, and hence should charge nothing.

THE CAPITAL MARKET

The rate of interest is a price, not only for money loans, but for measuring the cost of future against present consumption. Like all prices, interest operates in a market where the forces of supply and demand are at work. And when an economy is fully employed, any one form of economic activity can be taken up only at the expense of others.

There is, of course, a distinct element of choice about whether to abstain now in order to have more later on, or not. Every person who considers taking out an endowment life insurance policy faces this particular problem of weighing present against

future. With a high interest rate, the future prospects rise relative to the present. With a low interest rate, there is less incentive to save; and with no interest at all, accumulation would certainly be considered hardly worth while by many people.

It is probably true, as I have written earlier, that interest does not influence savings behaviour very closely. A great deal of the accumulation of resources done in a modern community is by business firms through their reserve and depreciation accounts. These are not likely to be greatly affected by rises or falls of a percent or two in interest rates. But a drop to nothing at all would be a different matter, because savings involve risks.

Putting aside £100 may be prudent for some people, even if no interest may be earned. If, however, prices start to rise, the real purchasing power of the £100 is diminished, and the little hoard is whittled away. However, I grant that social crediters will feel they need not concern themselves with this sort of risk; in their view, as already explained, prices would not shift with a social credit administration. But I have shown that there is every reason to expect very serious inflation under social credit; if this were to happen, one part of the crediters' claims would certainly appear to come true. Holders of money titles to savings would find the real purchasing power of these so reduced, that society would appear to be freed of a heavy burden of debt. But even this would not bring about the dream of a debtless society; prices for non-money titles would probably soar, and purchasing power be transferred from money holders to owners of real resources, such as land, goods, and factories.

But if saving for one's own direct purposes is risky, lending without interest to other people becomes downright folly. The capital market exists to bring together those who are saving and those who want to invest or borrow. When a deal is made, the borrower assumes a debt, and the lender an asset. All debts are assets in this sense. But why should anyone lend to someone else without an interest inducement? He stands to get nothing better than his capital, unless prices fall—a contingency which usually means depressed business conditions such as will render repayment difficult and unlikely. But he does stand to lose a good deal; investment is by no means a foolproof process.

A valuable institution of society, whereby people who want to save are brought into business relations with those who want to borrow, should not be lightly tossed aside. The interest payments

are protected by proper estimations of the productivity of the investment and adequate depreciations. The debts are matched by assets.

It is, of course, quite true that not all investments succeed. Governments are in a difficult position here. They must borrow and spend on projects which are difficult to measure in direct terms of financial benefit. And no Government can go bankrupt, a method open to private business as a means of writing off a mistaken piece of enterprise.

This difficulty of Government shows very clearly when war finance is considered. The huge costs of a modern war make financing it out of current taxes alone virtually impossible. Borrowing is a necessary evil; certainly it should be kept as low as possible. And wars are not productive in the ordinary sense as, say, a new hydro-electric scheme is. It is, however, usually agreed, especially during the war itself, that the aims for which one fights, in the broadest social sense, are worth fighting for and paying for. If peaceful existence can be regarded as worth a continuing 'insurance' type of charge, interest payments on war debts are justifiable, even if the assets which might match them have been blown out of the mouths of guns. And internally held war debts do not change the income of the country *as a whole*; they are merely transfers from the taxpayer in general to the stockholder in particular. External payments are not so easily dealt with, but the position there has rapidly improved for New Zealand, as will be shown when statistics are given in the next section.

I know that the payment of interest on the Public Debt is a matter of concern to the public, especially when it is on account of past wars. But the gravity of the situation may easily be exaggerated. And people should realize that criticism of this sort is really a criticism of war itself, not of the process of lending at interest, which is so useful a device for our economic life.

And finally, I should mention the view, which has some public support, that all public borrowing is wrong, as it piles up debts and interest dues. The young married man who wants a house does not regard it as wrong to borrow for it, and society would, I think, generally agree with him. It is not borrowing itself which is a crime; it is the circumstances under which the borrowing is done that matter. And these are usually special cases, to be judged on their merits, and not to be condemned out of

hand. As a personal assertion, which is all space allows me room for, I must state that I see no reasonable escape from borrowing for the New Zealand Government today. The country is growing fast, and has urgent needs for capital works. Funds, both from within New Zealand and abroad, are necessary to meet the demands which, remember, are forced upon the Government by the public.

FACTS AND FIGURES

Much play has been made by the social credit movement with the question of public indebtedness. (I am not sure whether they are equally concerned with private indebtedness.) The young New Zealander is pictured as being born into a world of travail, loaded up for his journey through life with an immense burden of past extravagances. It is not pointed out that he is similarly born into a world of existing assets: roads, buildings, railways, schools, power schemes and the like, which are there to be used in helping to pay for the burden. For, by and large, debts are held against existing assets. As long as the asset is productive, the debt item is not paid off, even if it is fully owned by whoever operates the asset. A farmer who has the freehold of his own property must surely calculate that, as a producer, he owes himself rent as an owner. This is fully recognized by the accounting convention which places 'capital' as a liability to a firm, and balances it against the actual physical resources, which are assets.

A child born into a debt-free world is a child born into a world without assets, or stored up wealth. The early Canterbury settlers plunged into debt for their Lyttelton tunnel. They presented posterity not only with an interest bill: they left the tunnel, too. And so, here is the paradox: indebtedness is likely to be a measure of wealth for the whole community. The real question is not how much debt there is, but how much providence and wisdom were shown in making the investments. It is the fallibility of man, and not the institution of borrowing, that should come into the searchlight of our criticisms.

Nevertheless, because of the special problems of Government, already indicated, arising out of productivity, war debts, and the inability to refuse to pay, it is certainly true that our public

debts should be watched with care. And social crediters have waxed extremely gloomy over the 'intolerable burden' of these piled up liabilities. So let us look at the actual record:

TABLE I

Interest paid on general Government Debt: £ millions.

Year	1938/9	'43/4	'46/7	'48/9	'49/50	'50/1	'51/2	'52/3	'53/4*
Paid overseas ...	6.8	6.6	4.7	3.3	2.7	2.5	2.5	2.5	2.5
Paid in N.Z. ...	4.7	9.0	12.9	13.3	14.0	14.8	15.2	14.8	15.6
Total	11.5	15.6	17.6	16.6	16.7	17.3	17.7	17.3	18.1

The general features of this are a marked jump in the bill in the war years, which, however has since pretty well levelled off, and a heavy reduction in the overseas payments, a result of the repayment of debts in London to the tune of some £82 million, most of it since 1945.

But the true *relative* measure of the interest burden is only seen when it is compared with certain other totals.

TABLE II — £ MILLION

Comparison of Total Interest Bill and Total Taxation Collected.

Year	1938/39	'43/4	'46/7	'48/9	'49/50	'50/1	'51/2	'52/3	'53/4*
Interest Paid ...	11.5	15.6	17.6	16.6	16.7	17.3	17.7	17.3	18.1
Tax. Coll'ctd. ...	37.8	100.8	113.1	130.4	135.6	157.9	200.5	199.8	205.9
Interest as % of taxation ...	30.8	15.5	15.6	12.7	12.3	10.9	8.8	8.7	8.8

These figures surely provide a dash of common sense to counteract the prophesies of doom. Almost a third of our national tax revenue went to debt interest charges in 1938-39. In spite of borrowing for war purposes, the *relative* burden of interest halved as heavy taxation was brought to bear. The burden has fallen still further since the war, and levelled off at not much more than a quarter of the pre-war rate.

But that is not all. Much Government debt, as already pointed out, is backed by productive assets, which have earning power. In fact, of course, the Government, through its various agencies such as the Railways, the Airways Corporation, the Life Insurance Office and so on, is a vast trading organization. And this work of government returns revenue to the Public Account in the

* Estimate

shape of operating profits. Here is some of the public debt paying its dividends:

TABLE III — £ MILLIONS

Total Interest Paid and Government Trading Income.

Year	1938/39	'43/4	'46/7	'48/9	'49/50	'50/1	'51/2	'52/3	'53/4*
Interest Paid ...	11.5	15.6	17.6	16.6	16.7	17.3	17.7	17.3	18.1
Govt. Trading Income ...	5.4	13.3	10.7	8.3	9.6	12.1	15.0	13.8	18.8
Income as % of Interest Paid ...	47.6	85.3	60.8	50.0	57.5	70.1	85.3	79.8	103.8

In view of the amount of public debt held on account of assets such as schools, which pay no dividends in the ordinary sense, and war expenses, the record shows a very reassuring general position as regards production from government held assets.

A few more facts may strengthen this general argument. Since before the war, the interest bill has gone from £11.5 million to £18.1 million—slightly less than doubled.

During the same period, the following increases give useful comparisons:

Gross National Product	from £231 m. to £827 m.
Personal expenditure on consumer goods and services	from £162 m. to £522 m.
Wages	from £111 m. to £387 m.
Government education expenditure	from £4.2 m. to £17.3 m.
Government health expenditure	from £0.8 m. to £4.7 m.
Defence expenditure	from £2.1 m. to £28.1 m.
Social security benefits and pensions	from £7.7 m. to £57.8 m.

Perhaps at this point a warning should be given: these statistics give a very broad picture, and very general arguments of this sort are apt to be misleading: they may be made to say too much or too little. It is, however, true that the *relative* burden of public interest in this country has fallen very heavily. This is what might be expected when it is recalled that rising prices lower the burden of interest charges, which are usually fixed in money terms. And it should be fully apparent that the social credit references to 'economic bondage' and 'intolerable burdens' are just nonsense.

* Estimate

In fact, the position is disturbing for a reason precisely opposite to that given by social crediters. The lagging behind of debt and interest payments, far from being a source of gratification, gives grounds for concern. Remembering that debts stand against assets, the question arises whether public investment in New Zealand has kept pace with growth in other economic departments of our national life. There seems a general case to answer: no. The long list of badly needed road and rail developments, schools, public buildings, power facilities and other public utilities, communications, and the rest, supports this view. New Zealand is inclined to eat its cake and want to have it, too. But worse than that, many people want to believe the social credit argument that a slice of the cake should be free, anyway—that slice which represents public storing up for future production. It cannot be free, and today it is too small a slice.

QUESTIONS ASKED AND ANSWERED

1 *If the Government wished to issue interest free money, could it do so?*

Yes. It is not customary, of course, and there would be technical and legal difficulties, I imagine. But parliament is a sovereign body, and could compel the Reserve Bank to conform to its will.

2 *Why then, should we go on paying interest?*

The text answers this. Do not confuse a paper world with the real world of resources. Why should the Government command the services of labour and materials without applying to itself the criterion of price; that is, of ability to pay interest for productivity?

3 *Why, then, should not certain socially deserving objects, such as pensioners' cottages, be financed interest free?*

The difficulty would be to stop short at some generally acceptable definition of 'socially deserving'. In real terms, the men who build these cottages and the materials they use, have to be drawn from the general pool of goods and services. The 'no charge' principle is false in real terms, and a scramble for 'free' facilities would be inevitable. We would then pay for the 'free' benefits by higher prices on goods and services all round.

4 *Would the abolition of interest rates, assuming it were possible, affect many people?*

Do not delude yourselves that only a small class of wealthy receivers, and the banks, would be the only losers. Abolition of interest rates would almost certainly suspend the operation, in customary forms, of:

—land valuation and rents
—superannuation schemes
—savings bank deposits
—life insurance
—house owning and valuation
—hire purchase
—all borrowing or lending for any purpose.

5 *Is there such a thing as an 'ideal' rate of interest for any particular set of economic circumstances?*

Unfortunately, no. Rates vary according to the risk of the loan, the time at which the contract was made, the period before the capital may be redeemed, and a host of other things. At any given time, interest rates for this or that purpose may reflect very poorly what they ought to reflect—the necessary level to bring out the savings the community needs to make to finance the investments it is planning.

6 *Do the banks set interest rates at any levels they may choose?*

Far from it. Trading bank rates are entirely a matter for Government decision, as regards their minimum and maximum levels.

7 *Are interest rates in general, then, set by the Government?*

Within limits the Government can control rates. To handle them involves complicated policy decisions about government borrowing, the control of private borrowing for housing and industry, the supply of money, taxation, and other matters. There may be times when control of interest rates may only be achieved at too high a price in terms of some other condition. But, the level of interest rates in New Zealand is, in broad terms, an outcome of government policy. In spite of this, thrift and extravagance by the ordinary public are powerful forces the government has to work in with.

8 *Should the Government borrow within New Zealand for its development programme?*

The Government may get its finance from three home sources. It can tax it out of the public, it can borrow from the Reserve

or the Trading Banks, or it can borrow from the public. At times of heavy commitments for capital works, such as the present, taxation would have to be squeezed up far too high to meet the entire bill. Furthermore, when assets which will pay for themselves out of future revenue are being built, finance out of current taxation is an unnecessarily severe technique. Borrowing from the public, while it *could* be inflationary in the short run (see text, Part I) is a perfectly sound method of offsetting legitimate saving. Borrowing from the Reserve Bank is risky at times of full employment: it holds a distinct threat of inflation. Reserve Bank finance, like most Trading Bank finance, is suitable for temporary credit carry-overs only.

Present day conditions, on the whole, justify a policy of heavy Government borrowing. It is a delicate task to do this, as the Government so far has managed, without pushing the rate of interest up too far. But, apart from this general view, finance of development needs consideration as a series of problems connected with particular projects.

9 *Should we borrow from abroad?*

In special cases, yes. Our liabilities on account of overseas interest payments have fallen very heavily indeed over the past fifteen years. We can well afford to borrow, on present prospects, particularly to increase our productivity which, of course, itself ensures ability to repay.

10 *Does all this imply that New Zealand need not worry at all about interest bills and debt?*

No. Every borrowing project, private and public, must be given careful consideration in its own right, to ensure that it meets the public interest, or is productive, and is correctly estimated. We always face the risk of falling prices and the resultant increase in the interest burden. Not the least disaster a slump brings is this extra weight of fixed charges. The meaning of this for policy is clear: the interest burden cannot be disposed of by social credit means. The question of debt is a matter to be tackled along different lines: preserve the peace, and stop the heavy costs of war; and maintain stable or rising prices, along with full employment. This puts the question of interest into the largest spheres of public action, where it is easier to say what is wanted than to devise policies to achieve these ends.

4

THE PRIMROSE PATH

THE CONSPIRACY OF SILENCE

It is now time to turn from the more or less straight economics of matters concerning social credit to more general questions. But first, it may be useful to summarize the three main steps in the purely economic argument:

(i) The A plus B theorem leads to the deduction that purchasing power is insufficient.

(ii) More purchasing power must, therefore, be injected into the economy. The only way for such a social credit dividend to be introduced is through the money system. In order for this to be done satisfactorily, money has to be regarded as a 'single use' coupon, created and destroyed by banks of issue.

(iii) Finally, in order that the social credit dividend should be genuinely 'free', the new issues must not pay interest. This involves a somewhat vague attack upon the institutions of debt and interest, particularly in the public field.

I hope I have shown the falsities involved in the theories at all points. The trouble is that the whole foundation of social credit belief, the A plus B theorem, forces upon its adherents a wrong and contorted view of the working of an economy. They are driven to their very odd views of money and interest by the unsoundness of their basic conclusion. But if the A plus B theorem produces indigestions of a logical type, it appears to compensate by the strength of the emotional satisfactions it offers to those prepared to believe.

There is little doubt that acceptance of the theorem has, for dedicated social crediters, the force of a spiritual conversion. The theorem becomes an Article of Faith, inviolable and unquestioned. If mere facts do not fit it, the facts must be explained away. If

somebody asks inconvenient questions about where the extra goods are coming from, in our fully employed economy, to match the higher money incomes the Theorem promises, the question may be brushed aside as irrelevant—almost, in fact, irreverent. The Theorem says that there is a 'gap'; fill it with money, the flow of money will match the flow of goods. How, then, can there be inflation? Why trouble about the extra production? Stick to the truth of the 'gap' and do not doubt. So argues the crediter, strong in the grip of his satisfying inner revelation.

And, like most bearers of a new Faith, the convinced social crediter must go forth to make new converts, to spread the good news of the economic gospel. And here he runs into a difficulty. For there exists a stubborn group of people—bankers, economists and the like, who deny the force of the Theorem.

It does not appear to occur to the social crediter that he might consider the Theorem according to whether it is right or wrong, whether it is logically consistent as a proposition, or plausible in terms of what actually happens. The Theorem is right, there is no doubt about it at all. He is, therefore, left with only two attitudes regarding the impenitently unconverted.

The bankers, economists, and others concerned may not understand the proposition, and hence merely be part of the great mass of unenlightened. It is difficult to maintain this about people who have devoted considerable abilities and full professional lives to the consideration of economic problems. The Douglas theory has had a long history now, and ample time has elapsed for its consideration, especially during the last slump, when professional economists were deeply concerned about 'under-consumption', and what might give rise to it. It can hardly be argued that a meritorious theory which achieved plenty of publicity would be overlooked or misunderstood by all. For the social crediter considers his Theorem as suitable for the ordinary man both to comprehend, and to cast his vote upon.

So another explanation has to be found. The Theorem, in this case, becomes a form of social dynamite to be concealed and suppressed, at all costs, in the interests of a small group of vaguely designated Bankers and International Financiers.

The 'gap' becomes a means through which the financially cunning can chisel from society a considerable slice of wealth. To preserve this state of affairs, an organized conspiracy of silence turns a stony ear upon the voice of truth.

In case this seems too much, I quote from Mr Owen: 'Tim Jones and Bill Smith . . . are so deliberately and consciously uneducated and miseducated that they blame politicians because no reform ever comes out of the changes of parties they keep sending to Parliament'.

The intellectual and moral arrogance of this sort of thing leaves one breathless. Are there no honest men anywhere except within the social credit movement? Can this sinister conspiratorial group really exercise such enormous powers of control that minds are turned blank, and lips stilled everywhere, at their commands? Of course not. But the conspiracy is a good means of persuasion.

The ordinary man, in his vanity, can readily stand to be told that he is getting less of the material benefits of life than he deserves. He also derives some moral satisfaction from the tale that Somebody, a sinister and shadowy back room Ruler of the World, is, by, cunning and indirect means, filching some of his hard earned dues. His attention diverted from the faulty logic of social credit (and who wants to think hard about all these thorny problems, anyway?), the prospective social crediter can wallow in a vague and satisfying emotion of frustration and hatred.

Primitive peoples took it out on the Scapegoat; the Romans supplied bread and circuses; the Nazis offered up the Jews; the social crediters will throw you a Banker or two. But the use of minority groups to focus animosities and sharpen emotional attitudes, even a group as vaguely designated as the social crediters,' is bad—morally and politically. Persecuting such groups has always been a camouflage for the weaknesses of a regime, and a doctrine. It is so again in this case. 'The conspiracy theory of society', as it has been called, is a standard weapon in the armoury of dangerously oppressive doctrinal politics.

The real source of the danger, apart from the inhumanities often involved, lies in transforming a situation of reason into a situation of emotion. Criticize social credit theory, and the true believers will come back with abuse of orthodox economists or repressive Bankers. Use a factual argument, and the tables are turned with vague references to emotionally powerful words like the 'slump' or the 'gold standard'. Furthermore, all criticisms of social credit (they say), spring from the sinister conspiracy. This work, for example, will doubtless be castigated as one more manifestation of the Conspiracy, another dishonest attempt to blacken the shining virtues of what is right and good. It will never occur to a convinced social crediter that anyone else may share his own concern for the good of society if he be in any way connected with economics. At best, such a person is a fool: usually he has to be a liar, too.

THE SUPER-OPTIMISTS

The emotional rewards offered to those who can accept the Theorem do not stop short at the satisfying hatreds and criticisms of the existing order which are evoked. They proceed to an ineffable optimism about the world of plenty, which awaits only the filling of the 'gap' to present itself to all. After all, the social crediter has to emerge from his world of book-keeping entries and paper tickets at some point of his argument. So he takes a long dive, and comes up in a transformed society.

He can persuade himself of a state of ultimate plenty by simple assertion. Man, he avows, has, by his mastery of technology, the means to vastly increased wealth sitting right under his nose. Production is an economic problem already solved: what is wanted is more consuming power, which social credit alone can provide.

Mr Owen writes: 'The outstanding feature of the economic system today is its capacity to produce in abundance. We do not think it can be doubted for a moment that there is enough machinery and plant in existence to produce more than enough goods and services to satisfy the whole community.

The world could be glutted with goods if the orders for these goods could be backed with money'.

Once again, the social crediter is led into error by the Theorem; in this case the 'gap' is elevated into the principal problem for a mankind already assumed to be master of his struggle with Nature. It is difficult to deal seriously with such views, but people seem readily to persuade themselves that we are indeed only stopped by the Conspirators from almost limitless prosperity.

Consider New Zealand today, with your own knowledge of its productive facilities: roads, factories, harbours, labour supply and so on. Run through in your mind's eye what you would buy if your income were, say, doubled, in money terms—a much more modest goal than the almost infinite riches promised by Mr Owen.

Now proceed to envisage the actual expansion in productive capacity required to meet these needs, exercised simultaneously by everybody. Note that most factories are already working to

capacity; read in the papers the blandishments of employers searching desperately for labour; consider our pastures and farmlands, and the stock they carry and might carry. Note further the housing situation, the development problems connected with building material, sewerage, power, roading and the like. Remember, above all, that an economic system is a vast auction, in which we bid for resources. Picture this auction sale enlivened by a sudden marked increase in money purchasing power, put at the disposal of people by a social credit system which blandly assures us that, if the money is there, the goods to match it will turn up out of our vast potential for more output.

But surely, it has been productive capacity which has been the trouble since the war. How else, to name only one thing, can we account for the constant, embarrassing shortage of labour in so many industries?

In a wider sphere, the social credit theory again fails to make sense. Britain, we must suppose, endured the rationing of so many desirable commodities for years because people could not afford to buy the goods? Absurdity piles on absurdity, when one considers how heavily subsidized the British farmer has been, to induce him to produce more, while his produce has sold at less than cost in the shops.

How, too, does this optimism account for different standards of living among countries which are at least all alike in not practising social credit? The U.S.A. has a much higher living standard than Great Britain. This is due to better natural resources and more heavily capitalized labour—more horsepower per worker. This suggests that productive capacity has been more limited in Britain than the U.S. in the past. Why do these differences show at all, if the production problems have been solved, as Mr Owen asserts? Mr Owen's world is one of great riches blocked off by the non-acceptance of the Theorem. Why should this world show differences in standards? Or does Mr Owen suggest there is a smaller ' gap ' in the U.S. than in Britain, and a very big ' gap ' in the poor countries of the East?

It is, of course, true that countries which can afford to capitalize their labour have raised their productivity, and with it, their standards of living. Technological progress is undoubtedly a feature of our times, as it was of Victoria's. But progress is slow when measured against mankind's matchless ability to extend the range of his wants. Our aspirations, our hopes, our needs—

even our so-called necessities, all grow by what they feed on, material progress. We are doomed, most of us, by our very natures, to economic dissatisfaction. The world of plenty can only exist for a race of creatures who know when they have had enough; I do not recognize this as the human race.

A highly progressive economy in full blast may push up its outputs annually at around 4% per year compounding. This would double output as a whole in little over 20 years; the U.S.A. may perhaps be about in this class. More sober progress at around 2% compounding seems to characterize the New Zealand rate of growth. Britain may average about this under favourable circumstances. The poorer countries of Asia struggle to maintain subsistence levels of living. There are no short cuts out of poverty, and the world as a whole is still a very poor place, made a little poorer, from time to time, by the problems of economic organization which show themselves in slumps, unemployment and commodity gluts. But these do not measure any vast potential wealth; they indicate the complexity of economic problems, the difficulties of reading future needs, and a variety of special market problems. The way to progress lies not in turning on the tap of purchasing power and hoping for the best; it is in careful attention to the details of economic organization, and in the old fashioned recipe of using one's wits to produce more with less effort, which is not as easy as Mr Owen asserts.

'THE UNSOLVED RIDDLE OF SOCIAL JUSTICE'

The title of this section was used for a book by Stephen Leacock. It admirably expresses a fact, basic to all social organization, that man can only live in groups by paying a price in compromise, by seeking ways of fitting together the diverse ends and needs which different people in different circumstances express. For example, security is felt by many to be a desirable end of economic organization, and our laws reflect this; but we pay a price for our security in many ways—it may encourage laziness, greed, passivity and other ills. At the same time, man feels that material progress towards higher living standards is a good aim; but this can easily clash with security, in that the incentives to work which mark the keenly efficient societies may cut too deeply for the security-minded to put up with. We may get cheaper and better

shoes, say, only at the price of sacking the incompetent and ruining the shareholders in an inefficient firm or two.

And so we have somehow to devise means of compromise, whereby security does not impede progress, and vice versa. Similarly, clashes show in the interests of classes within a society; how big a slice should workers, or farmers, or management get? Or Government expenditure may be the issue; more roads may mean fewer schools; the Auckland Harbour Bridge may prejudice the Lyttelton Tunnel Road, and so on. There is a constant push-pull of forces in society which, in their economic forms, reflect the limitation which is what the word 'economic' means: simply, that there are not enough resources for everything, so that a process of choosing, or sharing, or rationing has to operate.

These forces coalesce in politics into party issues, and find their way into policy by that route. This or that point of view comes to be developed in the various aspects of Government; usually the issues are debatable from different points of view; both means and ends may be discussed, as in the perennial arguments about private enterprise versus socialism in one form or another. But it is safe to say one thing: that at no time will *all* individuals find a social organization which will seem to them good. There is no such thing as the perfect society.

But men, with their longing for perfectibility, with their Utopian visions tucked up their sleeves, have always resented and resisted the compromises forced upon them from the very nature of societies containing individuals with differing viewpoints. If only some way could be found of pleasing everybody, and of giving all things to all men! And here social credit comes to the rescue.

The world of plenty which lies behind the 'gap' resolves the discords and disharmonies which agitate society. Capital versus labour is a battle without meaning, when the productive resources of society are fully unleashed. The arguments about how to allot this or that portion of the taxpayers' funds lose their force when State funds reach full amplitude under social credit, with shrinking taxes and a big 'dividend'. 'Politics' as commonly understood comes to have no meaning. Nor does 'economics' nor even 'reform'. We are presented with a world buzzing with technological marvels, with plenty for all, divorced from its long history of compromise, struggle, poverty and bitterness.

The prospect is undeniably attractive. The social crediter finds himself the advocate for a millennium in which he may ignore the sharp edges of contemporary problems altogether. Political controversy passes him by; he need associate with no particular pressure groups of society. Nor need he offend anybody by identifying his interests with theirs, as against someone else's. The great cooling stream of extra purchasing power will wash away the rancours of political and economic strife. Security and progress can march together. The aims of social credit can read like a catalogue of all the idealistic thinking any or all of us have ever dwelt wistfully upon.

The economics are wrong; the technological vision is a gross parody of reality. But the emotional force of the vision carries the believer in the Theorem beyond these difficulties. The symbol of social credit is the key. Turn it in the lock, and the door is opened on the new world.

It would be pleasant to sympathize with the undoubted idealism which lies behind all this. But the truth is that Utopian promises based, as they must always be, on failure to take account of reality, are dangerous, and, at times, potent medicines. Political and social wisdom lies in facing the problems of society, and thinking about them in detail as well as generally. And reform almost always involves being cruel somewhere, in order to be kind somewhere else. There is no key, no magic formula for a better world. No change in technique is going to elevate us rapidly into a paradise on earth. Society is not a mechanism which can be tinkered with, like a clock or a car, in order to put it into running order.

And so it must be faced that social credit, a painless path to prosperity which will disturb no-one except these vague Conspirators, is a form of delusion, which, however, can gain considerable political strength by its idealistic promises and its evasion of the thorny questions of the day. Like many other forms of escapism, it threatens to cause more trouble than it can possibly cure. Good intentions are not enough.

THE THIRD PARTY

Social credit polled rather more than 11% of the votes cast at the recent (1954) elections in New Zealand. It is anybody's guess why these hundred thousand odd voters chose as they did.

But, on the face of it, the result was surprising, for the simple reason that an era of prosperity and inflation, such as this country has been experiencing, seems hardly a plausible background for a programme of reform based upon the social credit belief in under-consumption.

I find it hard to believe that many who voted for social credit were of the inner circle of converts to the Theorem. I am also sceptical about political vacuums, and the attractions of novelty in an election unremarkable for issues; third parties have had short shrift in New Zealand at other elections, and even though the times may have changed, it is unlikely they have changed as much as all that.

My own guess, therefore, is that the surprising success of social credit reflects one of the least desirable results of the Welfare State. An inevitable consequence of a system of State benefits is the elevation of the Government, in many people's minds, to a sort of standing as a super Santa Claus, pushing cash benefits as 'free' bounties across the Post Office counters, and subsidies through the grocers' shops. It is easy to forget that the Government is the people, and that public money is our own money. We get nothing 'free', taking ourselves as a whole community.

The attitude that the State pays up, among rejoicings, to favoured folk is misleading; social security is a vast mutual insurance scheme in which we all of us put in the premiums. But the idea of 'something for nothing' is an outgrowth of the system, and once this takes hold, it may well look for an extension of the beneficial 'gifts' and subsidies. This sort of thing has been encouraged at the last two elections by both the established parties, which have engaged in a certain rivalry as to who can hand out the most.

Voters become conditioned to this. Policy is ignored beside the vital question 'How much'? I shall not dwell on the folly of this; it is bad morally, economically, and politically, and may well threaten the genuinely important operations of our social security system. I am here concerned merely to point out that some State handouts have prepared the way for social credit as the biggest and best promiser of handouts yet to arrive. There is a moral here, and I hope it sinks in.

Yet another political aspect of social credit doubtless exercised its appeal. This was the social credit attack on party politics as such. To many people, the system whereby men go into Parliament, line up on opposite sides of the House, and carve all issues up into for and against— this system affronts their conception of human dignity and the freedom of individuals to treat a question upon its merits. A man ceases to be an individual, they reason; he becomes a vote only, a cipher in the process of ironing out matters into the 'party' shape.

But Government, like banking, is an art. Its forms in democratic countries have grown out of experience and necessity. This is particularly so in countries like our own, which have no set of rules, or Constitution, so that growth can evolve without undue restraints of a formal type. And the party system has come to be the accepted working form of democratic government. Its faults are obvious, much more so than its virtues.

The case cannot be made in detail, but these points should be considered. If parliamentarians follow their own noses on every issue, how would business get done? Imagine the endless debates to get the necessary majorities. In the end, concessions and compromises would have to be made to get sufficient uniformity for legislation to be enacted. It is the business of Government to govern; the work must go forward. This means that legislation needs an axe, not a scalpel. Group discipline is a necessary means to effective action.

Further, it is a basic democratic principle that a Government should be answerable to the people. A party can align its members, and its legislative programme provides something on which a 'yea' or 'nay' can be pronounced. But if all parliamentarians are to vote on every issue according to their own feelings at the time, what is to go before the voters? An untidy, incomprehensible miscellany of indecisive and contradictory actions; a confusion of attitudes which finally throws the vote into the hands of that subtly dangerous attribute, personality?

Many readers will be aware already of the unsatisfactory nature of too many parties, and weak party discipline. The recent situations in France demonstrate this very clearly. Equally, one party only, as in Russia, hardly provides a democratic form of government, as most of us wish to see it. Social credit in New Zealand seems to give a vague promise of both these systems: of a 'no-party' form, with members free to vote according to conscience on all matters except those affecting the Theorem, or perhaps of a one party system which is, oddly enough, likely to work in the same way as a no-party one.

It is, of course, quite unfair to suggest that social crediters are themselves anti-democratic. Here again the logic of the Theorem has them in its grip. Their interests are economic, but they are driven into politics because there is no other way for them to set the Theorem to work. Their apparent lack of interest in all matters outside the narrow economic area of income flows confirms this. The vast miscellany of day to day matters, upon which ordinary parties feel compelled to state points of view, are of no interest to the social crediter, who argues that these things may be very well left to members' consciences.

In fact, social credit policy is not political at all. It almost appears as though Government, in the social credit view, can be relegated to a minor role. A commission will be set up to declare the size of the 'gap'. Parliament will then, presumably, declare the national dividend for the year, as a party measure. Other matters are left open. The implication of this is that other matters will hardly be important. This is all part of the logic, already explained, which suggests that political problems will have little importance, anyhow, once the situation of under consumption is put right. Truly, the load piled on to that Theorem is a formidable one.

QUESTIONS ASKED, AND PROBABLY UNANSWERABLE

A very pertinent question may have been forming itself in the backs of readers' minds. 'If social credit theory is as open to criticism as your enquiry appears to suggest', some may ask, 'Why has the movement persisted for so long, and made its weight felt so effectively at the recently elections?'

The reason is that social credit theory inhabits an intellectual thicket from which it is hard to drive it out. Matters concerning income flows, money, the trade cycle, and so on are intrinsically difficult. Several different 'worlds' are involved—one of income flows, one of money, one of debts, one of real goods and services. Simple leading questions can so rapidly lead to complications that the social crediter soon disappears in a cloud of confusion and misunderstandings. The plain man, unused to thinking in abstract economic forms, grows worried, baffled and hopeless; he ceases pursuing the question, and is left with the uncertain feeling that maybe there is something in what social credit says,

after all. Those who have followed this text with attention will realize how confusing are simple questions such as: 'Do banks create credit?', 'Is bank credit inflationary?', 'Do banks create credit out of nothing?', 'Is money merely book-entries?'

What is wanted is a set of Ground Rules for questioning social crediters. I propose, therefore, the following:

(i) Nothing about social credit is proved by abuse of the present system. It is not whether we suffered during the slump that is at issue; it is whether the social credit technique is a cure.

(ii) A general switching on of emotional reactions, easily prompted by such terms as 'socialism', 'gold standards', 'Bretton Woods', 'Montagu Norman' and so on, diverts questions, and says nothing about the virtues of social credit.

(iii) Keep the discussion to contemporary New Zealand conditions. A historical 'point-to-point' through the follies and sufferings of the past leads matters off the track.

(iv) Persist in tracking down the alleged conspirators. Answer dark hints about International Financiers by highly specific questions about who they are, what they do, where they live, and how they are to be dealt with.

(v) Alberta and British Columbia are not worth lengthy discussion; neither province practises social credit. Arguments about oil bounties and the like are, consequently, rather off the main line.

(vi) Keep the discussion within one 'world' at a time. For example, a question about money can be switched into income flows, over to real goods, and back into the paper world again, in most confusing fashion.

With these preliminary warnings, a set of assertions-cum-questions, classified according to the 'world' dealt with, may now prove helpful in approaching social crediters.

A *On the Flow of Incomes*

(i) Do you agree that all payments must be received by somebody? Payments, that is, are also receipts, depending what side of a transaction one is on.

(ii) All costs, therefore, are matched by incomes, if enough time is allowed for the process?

(iii) Do you agree that the 'gap' is on account of past payments, made in part against current output, and hence no longer available?

(iv) But would it not then be true that these past payments were made when they were not matched by output, i.e., they were, at the time they were made, additional to output?

(v) Is it not, then, always true that today's incomes are costed against a variety of goods: some already produced and consumed, some coming off the line today, and some not due for some time?

(vi) If, then, at any time, payments for output still to come are very heavy, purchasing power might be too strong. Surely this is possible?

(vii) The case of under-consumption, then, is likely to arise only when incomes generated in advance of production fall heavily?

(viii) Do you agree that savings cut down demand, and investment increases it, when both activities are as defined earlier in this work?

Note: The last three statements above clearly refer to the ebb and flow of purchasing power which may arise in a 'savings-dominated' or an 'investment dominated' world.

B *On the Quantity of Money*

(i) Would you agree that your theory requires money as a flow to match production as a flow, quantity for quantity?

(ii) You would further agree, I imagine, that this requires money to be destroyed after the single use of each unit?

(iii) Destruction of money may be achieved mainly by the following techniques:

(a) Cancelling a bank note.
(b) Reducing an overdraft.
(c) Sometimes, by running an import surplus.
(d) Transferring current to time deposits.
(e) Government sale of securities, with the proceeds used to reduce Reserve Bank demand liabilities.

The first two of these are the most important, as they will usually follow from the others.

(iv) Can Social Credit prove that *every transfer* of money leads to a destruction in the above sense?

(v) How can the social credit theory avoid the reduction of the overdraft of anybody who banks part of a social credit dividend?

(vi) Suppose the public confidence in money were shaken, and people started to pass it around more rapidly. Is this possible? If not, why not? Would prices remain unaffected?

(vii) Is it not true that most expenditure is merely a transfer of money, and not a creation or destruction of it?

(viii) The amount of money, relative to total annual incomes, varies greatly from country to country. How does social credit theory account for this?

(ix) New Zealanders hold, among other money savings, over £200 million in savings bank accounts. How would social credit digest this purchasing power into its matched flow of money and goods?

(x) How does social credit explain what would happen if:

(a) Everybody saved as hard as they could from today on;

or,

(b) Everybody spent as hard as they could from today on.

It is not impossible for such waves of spending and saving to develop. Consider a social credit injection of new money in relation to (b).

(xi) How does social credit expect to find the necessary sterling content for the extra purchasing power it proposes to create?

C *On Debts and Interest*

(i) Do social crediters advocate the entire abolition of interest rates throughout the economy?

(ii) If they do not, exactly where is the 'free' area to stop?

(iii) How does social credit propose to administer the 'interest-free' field?

(iv) Is any suggestion for this compatible with private enterprise?

(v) If repayment without interest is to be made, how long will this take? Who shall decide? What grounds will be taken into account?

(vi) Would social crediters agree that even 'interest-free' loans must draw real resources from the general supply, that is, compete with the 'paying' section?

(vii) How do social crediters show, statistically speaking, that public debt in New Zealand is growing intolerably? Do not forget to allow for the falling value of money over recent years.

(viii) Do social crediters agree that all debts are held by somebody, that is, are assets to somebody?

(ix) Would social crediters please support their allegations that the community is kept going by piling up bank debts, by a detailed statistical survey of banking in New Zealand?

D *On General Matters*

(i) Would social crediters please show in detail, with illustrations from New Zealand statistics, exactly how the gap is computed, and what size it would be for a few illustrative years since the war?

(ii) Who would belong to the social credit commission set up to compute the size of the 'gap'?

(iii) How would the social credit 'free conscience' vote in parliament behave when confronted by an organized opposition?

(iv) Once a particular annual 'gap' is filled by a social credit dividend, how is the next one to be measured?

(v) How would social credit deal with a serious fall in our primary produce prices abroad, assuming, as in fact happened during the last slump, that import prices do not fall as much?

(vi) Does social credit envisage issuing any special forms of new money, such as certificates, stamps or the like?

(vii) What policy would social credit adopt over the repayment of the next government loan to fall due in New Zealand?

(viii) Would the social credit government use its national dividend to pay public servants?

(ix) Suppose the 'gap' closes. What groups would be reduced first, among dividend receivers?

(x) How are Trading Banks to continue under social credit?

(xi) In terms of goods and services, does social credit admit:
(a) It is possible to take out without putting in? (as at Roxburgh Hydro).
(b) It is possible to put in without taking out? If not, how does the community store for the future?

(xii) How is the matched flow of incomes, money and goods reconciled with the question above?

CONCLUSION

This study has been an exercise in relentless criticisms. Some readers may question this, asking whether, in fact, it is worthy for so much trouble to be devoted to proving a set of ideas to be wrong. Surely (I hear the chorus), one should aim to be constructive, not destructive?

There are two answers to this: in the first place I have tried, throughout the text, to fill in the holes made by my criticisms of social credit. Many of the general questions raised by these matters have been dealt with in explanations of the trade cycle, money and banking, and the working of interest rates. One big hole, however, has to remain unfilled: the perfect society, its wheels oiled with free flowing money, its technology pouring forth more than abundant material blessings, is a myth and a dream. We do better to concentrate upon whether to raise the rates a farthing to build that access bridge across Squatter's Creek.

But there a second more general point, about criticism itself as an attitude hampering to progress. It must be understood that the very nature of progress in men's thinking lies in criticism of whatever is proposed. The correct attitude to social credit, or any other theoretical set of propositions for that matter, is to try to prove them wrong. Some theories stand up to the intellectual battering-rams for a long time; others collapse at the first good push. The rubble of the old is rebuilt into the new, and so thought progresses.

Suppose social credit were to be left alone and not criticized, on the general grounds of 'constructive' encouragement for brave new thinkers. And suppose the country suffers a disastrous inflation to prove social credit was not, in fact, right. Surely trial and error on this scale is an expensive and foolish technique? It is much better to go to the utmost lengths to test the social credit propositions before a national trial, with all the risks implied, is launched.

And one last point before the case rests. I suppose it may be expected that this study will be attacked in the almost spiritual terms of fanatical devotion the Theorem commands from its believers. It is almost certain to be alleged that I am a lame apologist for the order of things as they are, a mouthpiece for the Conspirators, a slave to economic 'orthodoxy' (whatever that may mean: is not the Douglas movement itself a prime example of dedication to a theoretical orthodoxy?)—a reactionary opponent of reform in all or any shapes. And so it may anticipate trouble to point out that none of these things is true. I am not a Conspirator, nor, if my work is studied with an open mind, will my conclusions be found to be anti-reformist in any way.

In fact, this is the constructive lesson I have tried to teach: the problems of economic institutions, their working in society, and their changes, are open questions. These institutions must take their shapes according to what men consider to be good or bad as social ends. But, as ends and means are easily confused, and the objects of reform must always be to some extent ambiguous, the working evolution of society must usually be a hotchpotch of compromises, opportunism, and expediency in terms of custom. This is more likely to be true of democracy, as we understand it, than of the totalitarian regimes, which can give a surface polish to social efficiency which often appeals to the mindless.

It is not enough to want a better world; the quality of the means must conform to the nobility of the ends, where reform is in prospect. In this regard, the social credit movement fails.

ERRATUM

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